

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

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UNITED STATES OF AMERICA
STATE OF CONNECTICUT,
STATE OF IOWA,
STATE OF MARYLAND,
STATE OF MICHIGAN,
STATE OF MISSOURI,
STATE OF OHIO, and
STATE OF TEXAS

Plaintiffs

:

10-CV-4496 (NGG) (RER)

-against-

:

U.S. Courthouse
Brooklyn, N.Y.

AMERICAN EXPRESS COMPANY,
AMERICAN EXPRESS TRAVEL
RELATED SERVICES COMPANY, INC.
MASTERCARD INTERNATIONAL
INCORPORATED, and
VISA INC.

Defendants

:

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IN RE AMERICAN EXPRESS
ANTI-STEERING RULES ANTITRUST :
LITIGATION (II)

11-MD-2221 (NGG) (RER)

- - - - - X

Thursday, October 9, 2014
10:00 a.m.

BEFORE:

HONORABLE NICHOLAS G. GARAUFIS
United States District Judge

Court Reporter: VICTORIA A. TORRES BUTLER
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Brooklyn, New York 11201
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1 (In open court.)

2 (Judge NICHOLAS G. GARAUFIS enters the courtroom.)

3 THE COURTROOM DEPUTY: All rise.

4 THE COURT: Please, be seated.

5 THE COURTROOM DEPUTY: Civil call for oral argument.

6 Counsel, just state your appearances.

7 MR. CONRATH: Good morning, Your Honor.

8 Craig Conrath for the United States.

9 THE COURT: Good morning.

10 You can go round the table.

11 MR. HAMER: Mark Hamer for the United States.

12 MR. BENNETT: Good morning, Your Honor.

13 Seth Bennett for the United States.

14 MR. KIM: Ihan Kim for the United States.

15 MR. CARTER: Thomas Carter for the United States.

16 MR. RYAN: Mark Ryan for the United States,

17 Your Honor.

18 MR. EWALT: Good morning.

19 Andrew Ewalt for the United States.

20 MR. GLASS: Ethan Glass for the United States.

21 THE COURT: Mr. Glass, good morning.

22 MR. GLASS: Good morning, Your Honor.

23 MR. GENTILE: Mitch Gentile for the Plaintiff

24 States.

25 MR. CHESLER: Good morning, Your Honor.

1 Evan Chesler for American Express.

2 MR. ORSINI: Good morning, Your Honor.

3 Kevin Orsini for American Express.

4 MR. FLEXNER: Good morning, Your Honor.

5 Donald Flexner for American Express.

6 MR. BRENNER: Good morning, Your Honor.

7 Eric Brenner for American Express.

8 MR. KOROLOGOS: Good morning.

9 Philip Korologos for American Express.

10 MR. WEISS: Jesse Weiss for American Express.

11 MR. CALIFANO: Good morning, Your Honor.

12 Mark Califano for American Express.

13 MR. BARBER: Good morning, Your Honor.

14 Peter Barber for American Express.

15 THE COURT: And Mr. Bright.

16 MR. BRIGHT: Well, good morning, Your Honor.

17 Gunther Bright, American Express.

18 THE COURT: Good morning, everybody.

19 This morning, we are going to have up to four hours
20 of oral argument by the parties. I don't have a clock;
21 sometimes we put up a clock, but I am going to ask you to keep
22 an eye on the clock yourselves so that we don't go over time.

23 For the plaintiffs, I understand that Mr. Gentile is
24 going to speak first; is that right?

25 MR. GENTILE: No, not first.

1 MR. CONRATH: I think I speak first, Your Honor.

2 THE COURT: All right.

3 MR. GENTILE: I just have three minutes after he's
4 done speaking.

5 THE COURT: Okay, that's fine.

6 Then, you are going to reserve some time for
7 rebuttal; is that right?

8 MR. CONRATH: Yes, I hope to, Your Honor. I will
9 reserve the remainder. Let's say, I hope it's about 15
10 minutes.

11 THE COURT: Okay.

12 And then who is going to speak for the Defense?

13 MR. CHESLER: I will, Your Honor.

14 THE COURT: Okay. Thank you.

15 Is anyone going to be using any visual aid?

16 MR. CONRATH: We have slides, Your Honor.

17 THE COURT: We have to make sure that we have them
18 in the record as well.

19 MR. CONRATH: Okay.

20 THE COURT: So, we need a copy for the record.
21 How about the Defense?

22 MR. CHESLER: We will also be using some,
23 Your Honor.

24 THE COURT: Okay, very good.

25 MR. CONRATH: I should add that the slides, the

1 electronic version of our slides is public. The hardcopy
2 contains the full material where there have been some
3 redactions for confidentiality reasons.

4 THE COURT: Okay.

5 Are we all set to go with the visual aid?

6 MR. BENNETT: Yes, we are, Your Honor.

7 MR. CHESLER: Your Honor, may I just ask a logistics
8 question?

9 THE COURT: Of course.

10 MR. CHESLER: As I think happened during the
11 openings as well, given the amount of time, the Government
12 will have one contiguous period of time for their closing and
13 I am just interested in the Court's preference because we may
14 get to a situation where, in the middle of my comments, we get
15 to a lunch break and I would rather do it without a break.

16 THE COURT: I have been thinking about that. What I
17 would like to do is take lunch at the end of the Government's
18 initial presentation and then we will come back after lunch
19 and have your presentation. We will have an early lunch, in
20 other words.

21 MR. CHESLER: All right.

22 THE COURT: And then we will have any rebuttal at
23 that point. I think that would be a better way instead of
24 breaking up your presentation into two parts, unless you feel
25 otherwise.

1 MR. CHESLER: No, I much prefer the way Your Honor's
2 going to do it, thank you.

3 THE COURT: That was my intention, I'm glad you
4 inquired.

5 Okay, Mr. Conrath.

6 MR. CONRATH: All right.

7 THE COURT: You may proceed.

8 MR. CONRATH: Thank you, Your Honor.

9 SUMMATION

10 BY MR. CONRATH:

11 MR. CONRATH: Good morning again, and may it please
12 the Court.

13 I want to start by thanking the Court and all of its
14 staff for the many courtesies that have been extended to us
15 throughout the course of this case and thank the Court as well
16 for making time available for us to have a six-week trial.

17 It turned out that trial gave us the opportunity to
18 learn a lot about this case. We needed those six weeks. We
19 had 38 witnesses, 19 merchants, we heard from all four of the
20 card networks, including 12 American Express witnesses and the
21 Court heard from four experts.

22 THE COURT: Can I just interrupt for a moment?

23 MR. CONRATH: Yes, certainly.

24 THE COURT: The six-week trial also afforded you a
25 window into the position and the strengths and weaknesses of

1 each other's cases.

2 MR. CONRATH: Yes.

3 THE COURT: And in doing the post-trial briefing,
4 you also gained certain insights, I'm sure.

5 Has that provided a tool for possible resolution of
6 this case short of a court decision? Has anything happened in
7 that regard? I will ask both sides to comment on that now,
8 that I am not counting that against your time. I am counting
9 that in favor of my future.

10 MR. CONRATH: No, nothing has happened in that
11 regard, Your Honor. I mean, as the Court knows, we originally
12 sued Visa, MasterCard and American Express. Two of them
13 settled. So it is, in principle, a settleable case.

14 THE COURT: All right.

15 MR. CONRATH: But nothing has happened in that
16 regard.

17 THE COURT: Well, I would just say, again, that if
18 there is -- and we have a senior representative of
19 American Express here, as well as Counsel -- that if there is
20 some opportunity for a viable settlement of the case, it
21 should be pursued as I go forward with reaching a decision.

22 I will get further into the process of reaching a
23 decision later on after I have heard from both sides, but it
24 is my hope that if there is some possibility of reopening
25 discussions on that subject, that you will take advantage of

1 it, all right?

2 MR. CONRATH: All right. Thank you, Your Honor.
3 We're certainly willing, should there be some interest.

4 THE COURT: Okay, go ahead.

5 MR. CONRATH: All right.

6 Your Honor, one of the things we learned from
7 hearing from all those witnesses is that this market is
8 broken. Christopher Priebe of Southwest Airlines you will
9 recall said that and it pretty much sums up what the evidence
10 shows.

11 This market is broken because there is no price
12 competition among credit card networks on merchant discount
13 rates. The normal competitive pricing mechanism is broken.
14 Normally, if you have a lower price, you can expect to make
15 more sales as a result, but this market does not work that
16 way.

17 The result is the competitors in the market do not
18 have any incentive to offer low prices. Jack Funda of
19 American Express expressed it quite clearly. I don't think
20 it's anybody's business strategy to be cheaper than the next
21 guy so no, we don't compete on costs, he testified.

22 And it's important to note, he said, it isn't
23 anybody's strategy to be cheaper than the other guy. What's
24 broken is broken for all competitors. It's broken
25 market-wide.

1 What does that mean? Well, as Mr. Hochschild of
2 Discover explained, it means that a strategy of low prices for
3 merchants is not viable because the merchants cannot shift
4 sale to the low cost competitor. There is one thing that the
5 evidence at trial made clear is that there is no price
6 competition among credit card networks on merchant discount
7 rates.

8 There is something else about which the evidence is
9 clear. Merchant steering works. Amex said that in its
10 post-trial brief. If merchants were free to steer customers,
11 then there would be merchants would be able to move some
12 sales. What that means is that the connection between low
13 prices and more sales, more business, would be restored and
14 that critical part of the price setting mechanism could work
15 again.

16 Mr. Funda explained what would happen if merchant
17 steering were allowed. Amex would have to compete harder both
18 for merchants and for cardholders. He said what would happen
19 if the anti-steering rules weren't there would be we would be
20 fighting to retain the business by any means necessary. We
21 may need to increase incentives to consumers, we may need to
22 reduce pricing to merchants.

23 And Mr. Priebe, from Southwest, said a similar
24 thing. He said if we had the right to steer, we would be able
25 to negotiate a better price.

1 So, there is no price competition among credit card
2 networks on merchant discount rates, merchant steering would
3 allow that competition. Amex's rules, that are the subject of
4 this case, block that merchant steering.

5 What, in general, does Amex say about those basic
6 propositions? There isn't a huge fight about exactly what
7 happened in the market. The fight is about what does it mean
8 legally. In broad terms, Amex has two categories of defenses.

9 One I might characterize as sort of technical
10 antitrust defenses; we didn't prove it enough, we didn't prove
11 it in the right way, there's some thresholds in the law,
12 that's one category of defenses I'll go through them in a
13 moment.

14 The other category is it's a good thing that we
15 blocked that competition. We can do something better and so
16 it's perfectly fine for to us block competition. I'm going to
17 address those issues next. But before I go on to those, let's
18 remember that this broken market is significant.

19 Merchants in the United States pay over \$50 billion
20 in credit card fees. You heard from merchants about how
21 credit card fees are one of their largest operating expenses.
22 Mr. Kimmet from Home Depot said that credit card fees cost
23 them almost as much as healthcare. Mr. Thiel from Alaska
24 Airlines said they pay in credit card fees twice what it cost
25 them for their airport employees. Mr. Holtey from Solitude

1 Ski Resort said that they spend more on credit card fees than
2 they do for the diesel fuel to groom their slopes. These
3 restraints matter because credit card fees matter, this broken
4 market matters.

5 What I'm going to do is discuss some of the main
6 points about the law and the evidence addressing both our
7 affirmative case and some of American Express's responses.

8 The Court is obviously familiar with the three-step
9 process for the Rule of Reason under Section 1, so I'm not
10 going to repeat that, but I am going to follow this process
11 step-by-step as I discuss it today. The first topic that I am
12 going to take up is the anticompetitive effects of
13 American Express's anti-steering rules.

14 First I want to touch on a few key legal principles
15 to keep in mind. It's important to remember that the
16 antitrust laws are designed primarily to protect interbrand
17 competition and that's exactly what this case is about. The
18 Amex anti-steering rules obstruct interbrand price
19 competition, the core thing that is protected by the antitrust
20 laws.

21 Second, to examine whether there are anticompetitive
22 effects on that competition under the Rule of Reason, as the
23 District Court in U.S. v Visa put it, you have to ask whether
24 the competitive process itself has been harmed and that same
25 principle was expressed by the Supreme Court in the Indiana

1 Federation case when it said that restraints harm competition
2 if they disrupt the proper functioning of the price setting
3 mechanism of the market.

4 Is that what's happened here? Yes, it is. The Amex
5 rules disrupt the proper functioning of the price setting
6 mechanism because they won't let a company who wants to have a
7 low price get a reward. The competitor who cuts prices can't
8 make more sales as a result. So, what's blocked by
9 American Express's rules is merchant steering. Merchant
10 steering at the point of sale.

11 We should remember that steering in all parts of the
12 economy is an everyday part of competition. Many merchants
13 came here and said that. They steer customers in the process
14 of competing in their businesses. Just one of them was John
15 Robinson from Ikea who explained that Ikea steers its
16 customers. It's part of how they compete.

17 Merchants also testified that if they were free to
18 do it, they would be able to steer in the future. They would
19 steer in a lot of different ways. Each merchant in a
20 different market in a different industry with a different
21 company had a different idea about how to do it reflecting the
22 competitive realities they face, but what they said was if we
23 had the freedom to do it, we could do it and it would make a
24 difference to us. They also, by the way, said they would
25 steer in a way to keep their customers happy so that their

1 customers will come back.

2 Now, Amex concedes some of the essential facts about
3 anticompetitive effects. On the question of is steering
4 blocked I hope the Court remembers Mr. Glass's many signs that
5 illustrated various types of steering and how what was not
6 allowed by American Express' rules.

7 And Mr. Funda confirmed that the effect of that is
8 that if anti-steering were allowed, American Express might
9 have to reduce prices. Amex also confirmed that it
10 aggressively enforces the rules even to the point of
11 terminating some merchants for noncompliance.

12 The upshot is the Amex rules mean that a credit card
13 network cannot cut prices and expect to increase the business
14 that it does. But cutting prices to increase business is the
15 very essence of competition. That's what this the Supreme
16 Court told us in Eastman Kodak Versus Image Tech. Cutting
17 prices to increase business is the very essence of competition
18 and that's what's blocked here.

19 And that's an important legal principle and the
20 Court heard it confirmed from merchant after merchant who said
21 that in other parts of their business where they have
22 competitive options, if they can offer increased business,
23 they can get a better price, but not here.

24 The Court also heard that in Mr. Hochschild of
25 Discover who said that in other markets that he's worked in if

1 you have a lower price, you can do more business. We asked
2 him, does that work in a credit card market? He said no, it
3 doesn't work that way for merchants. How does he know that?
4 Well, he knows it from experience. Discover's experience is
5 the first and maybe the best example of direct evidence of an
6 actual adverse effect on competition.

7 Discover tried to compete as the low cost,
8 simple-priced, merchant-friendly network. They offered lower
9 prices in exchange for more volume, major retailers were
10 interested and point of sale steering was essential for that
11 low price strategy to work. Why was merchant steering
12 essential for that low price strategy to work? Well, as
13 Mr. Hochschild explains in this excerpt it works because the
14 merchants' customers don't see the higher price. Only the
15 merchant sees the price and if the network is going to
16 increase its business in response by having a low price, the
17 merchant has to be able to encourage the customers to do
18 something about it, to use the low price card.

19 But that strategy was not allowed to Mr. Hochschild
20 and Discover because of the anti-steering rules, at that time
21 of all three companies. And Mr. Hochschild explained, he
22 testified. What did you do? Well, basically, their response
23 was if you can't beat them, we might as well join them and
24 they raised their price up to the level of approximately Visa
25 and MasterCard.

1 You can see that here in this next slide. This is
2 an internal Discover slide. It shows what happened because
3 the price mechanism was disrupted. The price increased. You
4 can see the low cost period and the closed competitive gap
5 period. The price goes up.

6 What you see in this slide is direct evidence. It's
7 direct evidence of what happens when there's harm to the
8 competitive process. It is also direct evidence of increased
9 prices as a result of that harm to competition. These are
10 Discover's prices. They went up because of the restraints on
11 competition that wouldn't let them succeed with the lower
12 prices. That's a price effect. It's direct evidence. It's
13 empirical evidence.

14 This is also evidence of a price effect because of
15 what did not happen. The other three networks did not have to
16 respond to Discover's low price competition as Professor Katz
17 explain to the Court. The other networks didn't have to say
18 oh my gosh, we're losing business, Discover's been increasing
19 its business, what are we going to do about it? They were
20 insulated from that price competition and that, too, is a
21 price effect of restricted competition.

22 This is not just a price effect in the past, it's a
23 current effect and a future effect. Mr. Hochschild testified
24 that if merchants obtain the freedom to steer, then Discover
25 would aggressively pursue a strategy of lowering our prices

1 and giving incentive to merchants that would steer incremental
2 volume to Discover.

3 THE COURT: Well, hasn't there been a change in the
4 pricing structure of the different cards so that at present
5 the cards are at about the same pricing level overall with the
6 these premium cards that Visa and MasterCard are promoting,
7 and so in terms of the current market situation, is there
8 really a difference among the cards in terms of overall
9 discount rates?

10 MR. CONRATH: So, there is much less difference than
11 there was at some points in the past, that's for sure. And
12 why is that? Why is that? Because the card networks didn't
13 have anything to gain by being the cheaper guy. They didn't
14 have anything to gain by being the cheaper guy. So, what you
15 saw is Amex at the highest rates, as they've talked about,
16 Visa and MasterCard were moving up their rates in part by
17 offering these rates because that was where all the
18 competition was channelled; there was no way for a network to
19 benefit from being the lower priced guy.

20 And it's true that if you take a look today, would a
21 merchant encourage a single -- be able to gain a lot of money
22 by moving people among cards at current rates. But
23 competition is a dynamic process. So, the reason that we're
24 asking for this relief is so that merchants can go to networks
25 and say hey, we can give you more business; if you'll cut your

1 price, we can give you increased business and that's the way
2 the competitive process should work. We don't have to be in a
3 world where all of them have the same high prices. If there's
4 competition, there's room for those prices to come down.

5 THE COURT: It can also be because the other card
6 networks have decided that Amex's strategy is good business.

7 MR. CONRATH: Well, certainly, you can see why they
8 would say it's good business in the environment where it
9 doesn't gain you anything to be the cheap guy. That's
10 certainly right, it makes perfect sense. If I don't get
11 anything by being cheaper, why don't I be more expensive?
12 That's what Mr. Hochschild said in the earlier period. We've
13 tried really hard to be the cheap guy, it's not working so
14 we'd better do something else. That's part of why the market
15 is broken, because there's no way for a network to do that.

16 And the antitrust laws aren't about dictating a
17 particular price or saying you need to have this price, you
18 need to have this outcome. They're about getting to the
19 outcome as a result of a competitive process. The antitrust
20 laws say if we remove the restraints on competition, the
21 market will find its level. And now there's a lot of evidence
22 in the record here that as a result of these rules, prices are
23 higher today than they would otherwise be, but the violation
24 is that they got there as a result of a process where
25 competition was broken, was impeded by the rules.

1 THE COURT: Isn't it possible that this can be
2 resolved through market forces in an age where you've got
3 impending competition from let's say, PayPal working on a
4 different model from the charge or credit card model and that
5 there may be a correction in the relationships without any
6 kind of court intervention?

7 I am looking for ways to avoid court intervention.

8 MR. CONRATH: Sure.

9 THE COURT: Because taking a conservative approach
10 where there are competing facts and it's difficult to sort
11 them out, which I will do if necessary, but I am asking
12 whether there is a way of self-correction in the marketplace
13 where the parties in this case, meaning Amex and the settling
14 parties, Visa and MasterCard, have to reassess their model of
15 operation, including the model that is used by Amex.

16 MR. CONRATH: Well, that is an appropriate question
17 to ask because intervention is a nontrivial act, of course,
18 and it makes perfect sense to ask that question.

19 The problem is that the anti-steering rules get in
20 the way of a lot of what might happen in the way of
21 developments to make the market more competitive. To make the
22 market more competitive you need to be able to differentiate
23 among the payment forms and among specifically, the credit
24 card networks.

25 So, you remember Mr. Hochschild was asked about

1 PayPal and he says they're an important merchant for us, but
2 for us they're a merchant. Merchants, they don't run a
3 separate network at all the different stores. They're, of
4 course, more important online, but there is no danger of, no
5 evidence in the record especially, that PayPal is in any
6 danger or that Visa and MasterCard are in any danger of being
7 replaced by any kind of the new payment forms that are
8 happening.

9 THE COURT: That was one of the, I think, implicitly
10 that was an argument being made by Amex, wasn't it?

11 MR. CONRATH: I think it was and I think that's why
12 I referred to evidence in the record. I don't think they even
13 put in evidence of what the current share of PayPal is, but
14 it's very, very small.

15 And the Court -- look. Nobody knows what's going to
16 happen in 20 years, that's right. But we have a record of
17 what the evidence is and what the market conditions are today
18 and that shows that the opportunity to grow by virtue of being
19 the low cost guy is blocked and that's the fundamental way
20 competition works.

21 The same thing is true about innovation. The way
22 you get rewarded for innovation. Just as more business is
23 your reward for being the low priced guy, it's also the reward
24 for being the innovative guy. So, if the anti-steering rules
25 block merchants moving someone to a new competitor, they also

1 block innovation. It's a topic that is on my list, but let me
2 talk about it now.

3 The Court recalls one of the possibilities that's
4 been thrown around is using mobile phones as a payment device.
5 Now, basically, at this point, those are wallets and they are
6 an electronic version of what's in your wallet. You pull out
7 your mobile phone and it's got your card on it instead of
8 pulling out your wallet and it's got the cards in it. It's not
9 new competition, it's a replacement for the wallet.

10 But, you will remember I think Mr. Priebe of
11 Southwest is on the Board of a group called MCX, which is a
12 consortium of merchants looking to innovate and find some way
13 to reduce and control their costs by doing something involving
14 mobile space.

15 What he says is we look at it, we need to be able to
16 do something to encourage people to use whatever we've set up.
17 We're very worried that we don't have the ability to do that
18 because anti-steering rules block anybody from moving volume.
19 So, if somebody comes along with a better idea, makes it
20 cheaper for merchants, how are they going to get steered to?

21 The answer is, you need the ability to differentiate
22 and that's why these anti-steering rules not only have blocked
23 past price competition, they're blocking current price
24 competition. They're also impeding the kind of innovation
25 that could make this market more competitive in the future.

1 I see my efficient colleagues have put the relevant
2 slide up. It's in the book at slide 24. This is some of the
3 innovation that's blocked; that the evidence in the record
4 shows has been blocked.

5 Discover had a Project Monet, which is a
6 merchant-owned network as a way for merchants to explore
7 having a lower priced option. Mr. Hochschild explained
8 couldn't get off the ground because they couldn't figure out
9 how to direct business to it in the face of the existing
10 anti-steering rules. MCX I talked about.

11 Sinclair Oil. The Court may recall Mr. Gibson of
12 Sinclair Oil and he said we've got this mobile app, it will
13 roll back the price at the pump at the moment depending on
14 what credit card and what the price of the credit card you've
15 got is. It's very innovative, a way to directly reflect price
16 increases, reward the company with lower prices and reward the
17 consumer for choosing a lower card. Can't use it now because
18 of the American Express anti-steering rules.

19 Official Payments talked about two things. You
20 remember Mr. Mitchell, when we finally got him here, was able
21 to explain that Official Payments had a workaround, their
22 ChoicePay site, and that making that work was impeded, he had
23 explained, he was worried about it being impeded in the future
24 by the Amex anti-steering rule and then there was the
25 testimony in the closed session where he talked about a new

1 technology that would directly benefit consumers and merchants
2 using price information and new technology that he was
3 developing.

4 Those are all examples of the innovation, record
5 evidence of innovation that's been affected by the rules.
6 That's in addition to the general principle that the way you
7 get rewarded for innovating is by getting more business. And
8 if merchants can't steer to you, that's going to reduce your
9 incentive to innovate and reduce the possibility that
10 innovation will get defused throughout the whole market.

11 So, it's a critical point for the Court to consider.
12 I think in light of the record evidence in this case, there is
13 no likelihood that at any time in the future, there is no
14 record evidence that there is some disruptive effect that is
15 going to wipe out the anticompetitive effects that we see
16 today and, in fact, the evidence says the innovation that
17 might make things better in this market is, if anything, going
18 to be impeded by the rules that are at issue in this case.

19 Let me talk just briefly about the other kinds of
20 direct evidence of price effect of an anticompetitive effect.
21 We're back on slide 19.

22 The Court will recall preference campaigns as
23 another category. This example goes back way in the
24 early '90s. Visa was a lot cheaper to merchants than Amex,
25 1.75 percent compared to 3.25 percent. Visa developed this

1 strategy, Mr. Morgan testified to you, about how to use that
2 price difference to encourage customers to use -- merchants to
3 encourage their customers to use the cheaper Visa card. They
4 developed this profit wheel and some signs saying we prefer
5 Visa. This was classic competition on price. Hey, do more
6 business with us because we're cheaper. Classic competition
7 on price. Competition on the merits. And it worked. Shares
8 shifted from Amex to Visa where the promotion was used.

9 Amex thought about how to respond. They considered
10 a long list of ideas including some pro-competitive responses
11 that included various ways to cut prices, but in the end they
12 decided on an anticompetitive response. They used their
13 anti-steering rules to shut down the preference campaign to
14 stop merchants from doing it and, as they said to themselves
15 internally, we thwarted this preference campaign.

16 Visa wasn't the only network to use a preference
17 campaign. In fact, the evidence shows that all four networks
18 used them at some point. Let's remember that MasterCard also
19 used it, using testimony from Ms. Biornstad. She talked about
20 how they had a deal with Travelocity for a preference. They
21 compensated Travelocity for that, which was a form of price
22 cut price competition. Amex came along and said no, no, no,
23 violates the rules, stop it. Travelocity had to stop it.
24 That price competition ended. More evidence of a direct price
25 effect. There was price competition. It was blocked.

1 I guess there's a side note I should mention because
2 Amex has talked a number of times about MasterCard as a part
3 of the duopoly with Visa. Of course, the Court knows we've
4 sued MasterCard twice, but it is important to remember just as
5 a factual matter, today Visa and MasterCard are no longer
6 joint ventures of this overlapping set of banks. The networks
7 were spun off into independent companies and that's the market
8 structure today. Mr. Morgan talked briefly about that.

9 Value recapture.

10 THE COURT: Do you think Amex would have survived in
11 the environment that existed when it initiated the NDPs if it
12 hadn't done so against the relatively high market share of
13 Visa and MasterCard? Was it really a defense mechanism to
14 permit them to survive and compete? And are we looking at
15 this through a 20/20 hindsight?

16 MR. CONRATH: I think it's always important to ask
17 yourself are we looking at what happened. It's easy to look
18 in hindsight, but I think the answer is yes.

19 THE COURT: Yes to what?

20 MR. CONRATH: Yes, they would have survived.

21 THE COURT: Oh.

22 MR. CONRATH: The other answer would have been a
23 little out of character.

24 THE COURT: No, I need a clear answer.

25 MR. CONRATH: No, no, to clarify, let me explain

1 why.

2 It's clear that there was some shift of share in
3 those places, especially those local markets where they used
4 this strategy, but there were a lot of other things going on.
5 The big picture here of what was going on was that Amex was
6 very strong in the travel and entertainment merchants.
7 Historically, that had been their strong point.

8 THE COURT: Are you going talk about the submarket
9 issue?

10 MR. CONRATH: I am.

11 THE COURT: Okay, go ahead.

12 MR. CONRATH: I could go there now.

13 THE COURT: I want to make sure we cover everything.
14 See, I don't have a structure. When I think of it, I ask.
15 Mr. Chesler will find out about that later.

16 MR. CONRATH: Well, I have a structure, I hope I
17 will get to all of it within the time allotted. I'm going to
18 do my best.

19 THE COURT: I teach at six.

20 MR. CONRATH: Well, maybe you should have said four.

21 So, Amex was very strong in T&E. Visa and
22 MasterCard were much stronger in sort of what we call the
23 everyday spend. Each of them was kind of moving into the
24 other's turf which naturally set off competition and they
25 probably both felt threatened by that for sure and it made an

1 effect.

2 And it's true that Amex had some troubles at that
3 time and I think -- I'm not sure I can remember all the
4 questions we went through on this topic, I think with
5 Mr. Chenault, perhaps -- I think that's correct, but Amex had
6 decided to introduce a credit card in addition to their charge
7 card services, the Optima, which they had a lot of troubles
8 with. It wasn't really successful, but it was another way
9 they were moving into the turf of the others. It was a good
10 thing, that's a pro-competitive thing, but it didn't go very
11 well for them for a while, so they had some troubles from
12 that.

13 And they were trying to be a financial supermarket,
14 something for everyone, which maybe put some pressure on the
15 management. I think Mr. Chenault acknowledged that they had a
16 bunch of problems, so American Express did have some rocky
17 period. The idea that it was all the result of the Visa
18 preference campaign, which is frankly, not supported by the
19 evidence in the record.

20 Also, if you look closely at the evidence on this
21 question, what was happening also is credit card use in the
22 economy generally was growing. So, it is true that
23 American Express's market share was declining, but the
24 reason -- and I think this is in Mr. Chenault's speech and
25 perhaps other evidence in the record, the speech that he

1 cited -- says that they were growing less slowly than Visa and
2 MasterCard. So, when I say they lost share, that's certainly
3 correct. That's not the same as saying they lost volume.
4 They were growing like this. Visa and MasterCard were growing
5 like this. That meant American Express's share was growing,
6 that's not the same as saying they were in danger of not
7 surviving.

8 Now, if they didn't react, if they didn't do what
9 Mr. Chenault came in and explained he did and was his job and
10 maybe is part of the reason why he's there today, because he
11 knew how to face a competitive challenge and respond to it,
12 what they did is they moved into everyday spend. His insight
13 was we can't survive as just a travel and entertainment card.
14 We need to move into the rest of the market. They did that.
15 They did that and that's why they succeeded and some of the
16 other travel and entertainment only cards didn't. But that
17 was a result of competition. They were competing and they
18 figured out a way to do it successfully and that's why they
19 are successful and today they're in every kind of business.

20 They have coverage of over 90 percent of the credit
21 card spending in the United States and that's why I say would
22 they have survived in the face of some merchants putting up
23 signs saying we prefer Visa? Yes, they would have had to
24 compete harder. Maybe they wouldn't have been able to keep a
25 3.25 percent as compared to 1.75 percent price differential

1 for as long as they did but sure, they could compete and
2 succeed in this market.

3 Let me just sum up on this, what's on slide 25.

4 What we've proved on the anticompetitive effect
5 point is that what's harm to the competitive process is a
6 broken link between cutting your price and increasing your
7 business. There was a direct effect on prices, prices went
8 up, Discover's prices went up, the other companies didn't have
9 to respond to Discover's prices. The price competition in the
10 form of preference campaigns existed, then it was stopped.
11 And there's also evidence of the harm to innovation which
12 eventually lead to a harm on output and quality. And this is
13 proved through merchants explaining it, all three competitors
14 explaining it, some concessions from Amex and also, expert
15 testimony.

16 And this effect was a market-wide effect. It's not
17 just a narrow effect on the percentage of the business that
18 Amex has because their rules are in marketplaces that cover
19 over 90 percent of credit card spend, the effect of these
20 rules is throughout the market.

21 So, what does Amex say about this? Well, the main
22 thing they have to say about this is to criticize the legal
23 standard that we're applying and say well, no, no, no, you're
24 relying on Indiana Federation of Dentists and you're using it
25 wrong. I'm going to tell you why that's not right.

1 Indiana Federation of Dentists, Supreme Court
2 confirmed that direct anticompetitive effects can be shown by
3 harm to the competitive process. Amex claims that that test
4 is only available for the quick-look type of antitrust
5 analysis, but Todd v. Exxon in this Circuit confirmed that
6 Indiana Federation is not limited to quick-look cases.

7 And then, Amex wants to say well, you can't rely on
8 looking at the harm to the competitive process, at least in a
9 vertical case without empirical evidence the prices would be
10 higher or quality would increase. Well, none of the cases
11 they cite for that proposition make that ruling. The cases
12 they cite looked at the evidence that was at issue in those
13 cases, but they did not say that was the only kind of possible
14 evidence that applies to Todd, KMB, Tops, Capital Imaging.

15 In any event, in this case the Court didn't have to
16 reach that because we proved price effects, we proved quality
17 and innovation effects far beyond the burden that's been
18 required in any case before this. There's concrete proof
19 actual competition that existed and was squelched, there's
20 plenty of hard facts in this case about anticompetitive effect
21 and so we meet whatever standard the Court concludes is the
22 correct one in this case.

23 THE COURT: Well, isn't American Express saying in
24 its post-trial papers that this is a two-sided market and
25 looking only at the discount rate only looks at one side of

1 the market, and what you really need to do and you haven't
2 done it, is to prove a net anticompetitive effect on both
3 sides of the market and they have a unique business strategy,
4 the value proposition strategy and that addresses both sides
5 of the market and you haven't done it, so you lose?

6 I think, in a nutshell.

7 MR. CONRATH: In a nutshell, that's their argument,
8 yes.

9 THE COURT: So, what about that?

10 MR. CONRATH: Okay. Well, let's go to page 68.

11 THE COURT: Oh, we're moving on.

12 MR. CONRATH: We're moving right along. We might
13 have to go back and touch some of those earlier pages if you
14 permit me the time.

15 THE COURT: You're talking about the anticompetitive
16 effect on one side of the market and they're saying you've got
17 to look at the whole picture.

18 Go ahead.

19 MR. CONRATH: So, let's talk about this because
20 really, they talked a lot about two-sidedness, they talked
21 about it in connection with market definition, competitive
22 effect and their justifications.

23

24 (Continued on following page.)

25

1 MR. CONRATH: So, here's the core of what they're
2 saying. It's all right if there's harm for merchants.
3 Merchants pay higher prices because of the restriction on
4 competition, but we can trump that because we say there's some
5 benefits to cardholders on this side.

6 There's no case that stands for that proposition.
7 No case. No cited case that stands for the proposition or
8 anything even remotely like that. No court has decided that
9 harm on one side of a two-sided platform can be offset by
10 benefits on the other side.

11 It is true that this market has two-sided
12 characteristics. It's a fact about the market and has to be
13 considered. Professor Katz testified he did it throughout his
14 testimony. Every market has particular facts that you've got
15 to consider. That's one of them in this market. But courts
16 have been considering two-sided industries for years using
17 regular antitrust tools that are, and not doing the kind of
18 revolutionary turning the analysis upside down that really is
19 what AMEX is asking here.

20 If you look, the Times Picayune is the first
21 quotation you have there which is a newspaper market everyone
22 recognizes is two-sided. What the court says is that every
23 newspaper is in two separate though interdependent markets and
24 it says this case only concerns one of those markets.

25 Now, AMEX tries -- so let's talk about market

1 definition first because AMEX tries to put the two side issues
2 into market definition and also talk about it in connection
3 with effects.

4 The way they try to put this into the market
5 definition question is to say that you should define a market
6 for transactions. That's their way of putting all the
7 two-sided issues in the market definition. It's also their
8 way of trying to make it part of the plaintiffs' burden. They
9 want to get credit for anything happening to cardholders by
10 putting it in the same market with merchants.

11 Now, this approach is wrong in the way of thinking
12 about market definition because they're insisting on putting
13 things into the market that are not reasonably interchangeable
14 and reasonable interchangeability is the litmus test for
15 market definition.

16 So we can understand what's wrong with this by
17 looking at two slides where AMEX describes the credit card
18 industry. One's in the ordinary course of business and one's
19 in this trial.

20 Let's take a look at the next slide. This is the
21 ordinary course of business document. This is a presentation
22 by Mr. Gilligan to the board of directors in 2010. It shows
23 how AMEX thinks about the credit card industry. You'll note
24 there are five entities on this chart. You've got the
25 cardholder down on the lower right, the card issuer, the

1 network, the acquirer and the merchant.

2 You can see on this chart the two separate markets
3 which are part of it that were defined by the court in U.S. v.
4 Visa. Markets that were in a minute, as we'll see, those two
5 markets would be lumped together by AMEX into a single market
6 for transactions the way they're, in what they're asking this
7 Court to do. You see the lines on the right there between
8 issuers and cardholders. That's what's going on in the market
9 for credit cards, the competition among issuers, AMEX and
10 banks, to provide cards to cardholders. That was one market
11 in U.S. v. Visa.

12 Now, look in the middle. The network there is
13 selling services to the card issuer and to the merchants and
14 you can see in this, one other feature of this presentation,
15 the kind of the light blue box that's around the issuer, the
16 network and the acquirer reflecting the fact that for some
17 transactions, AMEX itself is the issuer and for many
18 transactions, AMEX itself is the acquirer, it's always the
19 network for AMEX transactions, but it's true that AMEX also
20 deals with some third-party issuers like Wells Fargo Bank and,
21 as you heard testimony, it deals with some merchant acquirers,
22 it deals with merchants sometimes directly and sometimes
23 through acquirers.

24 When we look in the middle there, the network is
25 selling services to issuers and to merchants. The main focus

1 in U.S. v. Visa was competition among networks in selling
2 services to issuers, that was the restriction that we wanted
3 the court to stop, and that was the other market in USA v.
4 Visa, network services being sold to issuers. There's another
5 set of services sold to merchants as well. Notice what's in
6 these two markets is not interchangeable. If the cardholders
7 in the market for cards feel the price of credit cards is too
8 high, they can't decide to substitute some network services.
9 Those things are not interchangeable.

10 What AMEX wants to do with this market for
11 transactions is sweep together the competition among issuers
12 for cardholders and the competition among networks for issuers
13 along with the competition that's at issue in this case which
14 is the competition among networks for merchants all into one
15 market and we can see that on the next slide.

16 The next slide allows us to compare how AMEX
17 describes the market in this courtroom as compared with what
18 it was describing in the board room.

19 This slide is from Professor Gilbert's presentation.
20 It says at the top there, The product at issue is the
21 transaction. And when we asked Professor Gilbert about that,
22 he said what that means is the flow around this whole loop
23 between the consumers and merchants, this whole thing on the
24 slide. Professor Bernheim adopts that, that definition.

25 Well, what's wrong with that? Well, one of the

1 things that's wrong with that is it just, it combines things
2 that aren't interchangeable. If merchants face higher prices,
3 they can't substitute more credit cards. There's different
4 competitions going on, there's -- and that's why it ultimately
5 is right to define them as different markets. AMEX can point
6 to no court that has found anything like this as the relevant
7 market.

8 AMEX itself, let's remember, a few years ago,
9 alleged separate markets for network services and for card
10 issuance when it sued Visa and MasterCard and collected a
11 substantial settlement on that theory. So this claimed market
12 definition just doesn't add up. You see what's happening is
13 there is a lot of competition among issuers to sell cards to
14 cardholders. AMEX wants to take credit for that and say well,
15 therefore, you can ignore the fact that there isn't price
16 competition among networks for merchants, but one of those
17 does not offset the other because they're not interchangeable.
18 But AMEX raises this issue and pushes it also in the context
19 of the effects.

20 Let's talk about how to consider two-sidedness in a
21 legal framework and go through the possibilities. So, the
22 standard approach is quite direct, and it's what we think the
23 approach the Court should follow.

24 A two-sided platform, like a credit card network or
25 a newspaper, sells to two groups of customers. Each group of

1 customers is entitled to the benefits of competition, is
2 entitled to the protection of the Sherman Act. So, we are
3 here as a government enforcement case but imagine, and maybe
4 you can imagine it, a case where the merchants are the
5 plaintiffs, coming into court and saying we're injured by --

6 THE COURT: I have a case like that.

7 MR. CONRATH: I think you do.

8 -- we're injured, we're injured by a restriction on
9 competition. There's a direct harm on the price setting, a
10 direct restriction of the price setting mechanism and it hurts
11 us. What AMEX would have you say is sorry, merchants, there's
12 some other people, cardholders, they get a benefit, you don't
13 have to worry about it.

14 The antitrust laws protect competition wherever it
15 shows up and the way to think about the credit card industry
16 is, look, there are network services that are sold to issuers
17 and some of those get resold, then that is input in the
18 competition for cardholders. There are network services sold
19 to merchants and the merchants are entitled to the benefit of
20 that competition without saying cardholders are better off.

21 That's, we think, the right approach. It follows
22 Times Picayune. It doesn't involve any complicated putting
23 together of one kind of competition with a different kind of
24 competition.

25 THE COURT: Well, I think the other side is going to

1 say that they have a unique model and that it defies the
2 general analysis that you very clearly have posited.

3 What do you say about that?

4 MR. CONRATH: Okay. I saw a couple of things, so
5 hold with me here while I go through a couple.

6 THE COURT: No, go ahead. I'm just trying to move
7 on.

8 MR. CONRATH: I'm doing my best.

9 THE COURT: No, it raises the issue --

10 MR. CONRATH: It does. It does.

11 THE COURT: -- that they raise in response to the --

12 MR. CONRATH: Right.

13 THE COURT: -- you know, the case law that this is,
14 this may be, you know, we have now moved into new territory in
15 antitrust analysis. So unfortunately, it's in this
16 courtroom --

17 MR. CONRATH: Yes.

18 THE COURT: -- where we may be moving into that
19 territory, but I want to know what your response is to that
20 kind of argument.

21 MR. CONRATH: Well --

22 THE COURT: Go ahead. Do it in your own time.

23 MR. CONRATH: Let me take it at a high level and
24 then go back to where I was going to go. This is an important
25 issue. They're making a big deal of it and I want to take the

1 time to walk through it.

2 At a very high level, what they're saying is very
3 much, ah, this is a new thing, courts have never heard of it
4 in 120 years of the Sherman Act and you should do something
5 different. That is the essence of what they're saying,
6 something no court has ever done before, but what's the logic
7 behind that?

8 We've discovered something special that lets us
9 block the kind of competition that we don't like on price for
10 merchants, force all the competition in the market into the
11 kind of competition that we do like which is competition on
12 being, on rewards for cardholders, and we should get to do
13 that even though other firms might choose a different kind of
14 competition.

15 The AMEX -- if the antitrust laws stand for one
16 thing is that I, as a competitor, don't get to dictate how my
17 rivals compete and if you accept the argument that American
18 Express is making, that's what they're saying: We've got this
19 special model and we ought to be able to impose it on the
20 industry and make everybody try to be like us. The antitrust
21 laws just can't be warped that far out of shape because
22 they're about letting the market work. What the principle of
23 the antitrust law is not that we need a particular outcome, we
24 need a particular price. The principle is Congress said
25 competition is the rule of the day and we're going to trust

1 the market participants, in this case, we're going to trust
2 merchants, cardholders, networks, making free and independent
3 decisions to come up with an outcome. What AMEX is suggesting
4 is, no, no, if we've got an idea of how we want to compete, we
5 need to make sure nobody else can disrupt that, and that just,
6 you can't push the antitrust laws there. That's
7 protectionism, not competition.

8 There is a way, and I think what I first described
9 is the right way to think about this, but an alternative
10 finding the Court might consider making is to think about
11 considering these pro-competitive benefits that AMEX says it
12 can provide in the kind of standard framework of Section 1
13 analysis.

14 First, the plaintiff proves an adverse
15 anti-competitive effect. Defendant has an opportunity and the
16 burden to establish that there is some pro-competitive effects
17 that offset it. Normally, the normal rule would be those
18 pro-competitive effects ought to be in the same market, but if
19 those are to be considered, that's where they belong, that's
20 who the burden belongs on.

21 If the Court goes there, we should win anyway
22 because AMEX has failed to meet that burden. The evidence
23 that was produced at trial just doesn't prove what AMEX would
24 have to prove under that standard. The evidence shows that
25 the anti-steering rules harm competition among networks for

1 merchant business and lead to higher prices. AMEX hasn't
2 proved that the anti-steering rules generate enough benefits
3 on this other side to outweigh their anti-competitive arms.

4 They can't prove that because though some of these
5 facts are in the record and that steering rules increase cost
6 to merchants and merchants have to recover those costs from
7 all of their customers, not just the ones who pay with credit
8 cards. So all customers pay some higher prices reflecting the
9 high costs of credit cards including those who pay with no
10 rewards cards, with either debit cards, checks and cash. At
11 best, only AMEX cardholders or maybe other rewards cardholders
12 benefit from this kind of differentiated business model that
13 AMEX is telling you is the reason why you should do something
14 new and unprecedented.

15 AMEX offered no evidence, no evidence to explain how
16 the benefits that AMEX cardholders and other rewards
17 cardholders get offset the higher prices that are imposed on
18 the every day consumers of all the merchants who take American
19 Express credit cards in the form of higher retail prices.
20 They offered no evidence to try to explain how those are
21 offset.

22 (Continued on next page.)
23
24
25

1 (CONTINUING)

2 MR. CONRATH: And, let's think about some of the
3 other evidence. The evidence in the record shows that if we
4 think about what's the effect on cardholders and customers, if
5 merchant steering is allowed, sometimes cardholders and
6 customers are going to get a direct effect.

7 So, for example, I think we talked about an example
8 like this during trial, a customer goes in to Best Buy or
9 Sears and wants to buy a refrigerator, wants to use a credit
10 card. The customer, if merchant steering was allowed, might
11 get the choice, do I use my American Express card I'll get
12 some reward later and maybe that would be good for me or do I
13 use my Discover card? Maybe I can get 40 bucks off right now.

14 The customer, the customer doesn't get that choice
15 today. If the customer could get that choice, then the
16 customer could choose which do I value more? Do I value these
17 American Express rewards that I'm going to get later or do I
18 value the 40 bucks off today? That's a choice the customer
19 makes. It's a choice that's denied to the customer under the
20 current system.

21 THE COURT: Why is that denied to the customer as
22 long as the customer makes the choice without any prompting
23 from the merchant?

24 MR. CONRATH: Because the merchant can't offer him
25 the 40 bucks off.

1 THE COURT: You're saying 40 bucks off the --

2 MR. CONRATH: Refrigerator price.

3 THE COURT: -- purchase price as opposed to the
4 rebate that the Discover card permits.

5 MR. CONRATH: Right, right.

6 THE COURT: Okay, got it.

7 MR. CONRATH: The danger of using a concrete
8 example, Your Honor.

9 THE COURT: I understand now.

10 MR. CONRATH: If the merchant's trying to steer
11 customers to a lower priced card, one of the ways it might do
12 it is by offering a discount.

13 THE COURT: Right.

14 MR. CONRATH: The customer gets to make that choice.

15 So, the current rule by Amex doesn't let that
16 customer have that choice. Some customers might prefer the
17 immediate discount. So, if we're talking about what is the
18 net effect on the cardholder side of the market, we don't just
19 think of the Amex rewards as a total benefit because there's
20 this other effect. The customer doesn't get the immediate
21 benefit that he or she might have wanted.

22 Amex doesn't offer evidence that allows you to sort
23 out why it is that that loss of competition makes the customer
24 better off. Basically, Amex is saying we know what the
25 customer wants, they shouldn't have that choice and there's no

1 way they can meet the burden of establishing that that's a
2 pro-competitive benefit. It's an anticompetitive effect, in
3 fact, on the other side.

4 And finally, the other reason why Amex can't meet
5 this burden is that without the steering rules, merchants
6 would steer more frequently, as they explained at trial and
7 one of the things the issuers might do, including Amex, is
8 think what do I do if I want to make my cardholders less
9 amenable to steering? Well, one thing I might do is increase
10 their reward, make it more attractive to them.

11 Mr. Funda testified about this. That would be a
12 benefit to cardholders of more competition and American
13 Express has no explanation, no consideration of how it offsets
14 that, how that effect of their anti-steering rules, which is a
15 harm not only to issuers but to cardholders, they don't try to
16 offset that or explain why they meet their burden considering
17 the effect of their model.

18 There is a third possible approach, which I believe
19 is Amex's approach that it's incorrect. If I understand their
20 argument, they say that the burden on plaintiffs is not only
21 to prove that the anti-steering laws harm competition for
22 merchants, but also to disprove the idea that the
23 anti-steering rules generate offsetting benefits for
24 customers. So, they put all the burden on the plaintiff, not
25 only prove the harm to merchants, disprove the benefits to

1 merchants.

2 THE COURT: To?

3 MR. CONRATH: Benefit to cardholders.

4 THE COURT: Cardholders.

5 MR. CONRATH: Thank you, Your Honor.

6 First, let's point out they can't point to any case
7 that supports that proposition. This approach would
8 dramatically alter antitrust analysis in any market with a
9 two-sided platform; newspapers, real estate, software, in
10 addition to credit card industry. Even under this approach,
11 plaintiffs would prevail because the evidence that's in the
12 record actually enables the Court to find that the plaintiffs
13 have met this burden. Why is that?

14 Evidence in the record shows that the anti-steering
15 rules harm competition among networks for merchant business.
16 The effect of that is higher prices for networks. Amex does
17 not pass on all the revenue it takes from those higher prices
18 to its cardholders in the form of reward. Neither in total,
19 nor in a marginal basis; that is, every extra dollar it gets
20 in revenue for merchants gets passed on to cardholders. The
21 evidence does not establish this. In fact, it establishes
22 that it does not happen. Amex's CFO quoted by Professor Katz,
23 which he says is consistent with economic theory says if
24 merchant prices are higher, some of that's going go to Amex's
25 bottom line even if some it eventually goes to the

1 cardholders. So, what's the net effect?

2 If plaintiffs incorrectly have to prove the net
3 effect, what's the net effect? Higher prices for merchants,
4 only some of it is an offsetting benefit for cardholders. The
5 net effect, if you really have to add the net effect, is
6 overall harm on the two side of sides of this platform. So,
7 even under Amex's extreme and let me emphasize unwarranted
8 interpretation of the law, plaintiffs should prevail.

9 If you take the logic of Amex's approach just to see
10 what's wrong with it to its extreme, they're saying -- I mean,
11 it doesn't necessarily apply only to them. This is a
12 two-sided market for everybody. They're saying Visa could do
13 whatever it wants to stick it to merchants and as long as
14 there are benefits to cardholders, there's nothing anybody can
15 do about it. That's the logic of Amex's position.

16 Amex's view is, I think, based on the kind of a
17 fundamentally wrong idea that is not supported factually in
18 the record. It is that is there's some kind of inexorable
19 simple relationship between merchant prices and cardholder
20 benefits. Merchant prices go up, cardholder prices go down,
21 and the reverse.

22 Well, you can maybe write a theoretical model that
23 shows that but the real world is more complicated than that
24 because there's a lot of other competitive factors going on.
25 Just to mention a few, cardholder fees, interest income, how

1 broadly your card is spread out.

2 THE COURT: Well, you are leaving out shareholder
3 pressures.

4 MR. CONRATH: Yes.

5 THE COURT: The market, you know, there is another
6 market involved here and that is the stock market. This is
7 not a not-for-profit corporation where they are just passing
8 along long the benefits from the discount rate to the
9 cardholder in terms of reward. There is something in the
10 middle, too. So, I just point that out to you, that I
11 understand that as a consumer. You don't have to be a judge.
12 If you are alive in 2014, you understand that everyone has an
13 interest.

14 MR. CONRATH: Yes. Absolutely.

15 And Amex has to, absolutely has to figure out a way
16 to compete in a way that enables it to make a return to
17 shareholder.

18 THE COURT: That was mentioned in testimony as well.

19 MR. CONRATH: It's been mentioned in every antitrust
20 case I've ever been involved in, Your Honor.

21 THE COURT: I thought I had mention it here.

22 MR. CONRATH: We wouldn't want to let it go
23 unmentioned, I would feel disappointed.

24 THE COURT: Thank you.

25 MR. CONRATH: But it's important to take the context

1 of that because the idea that we get to block competition from
2 our rivals in order to earn more profits, it is not a
3 proposition that is defended in the antitrust laws. That is
4 what we have heard, I think.

5 I think, if I get down here a little ways, I'm going
6 to say that's what this comes down to. That's what this comes
7 down to. They're saying we need to be protected from
8 competition so that we can earn more profits and that's not a
9 defense that's cognizable under the antitrust laws. What
10 you're entitled to under the antitrust laws is the opportunity
11 to try your particular model, to try to offer your product.
12 You don't get a guarantee.

13 If the market doesn't respond, if merchants and
14 cardholders together, issuers, third-party business don't
15 accept your product, then you will face lower profits. If you
16 make something that merchants and other consumers really like,
17 you get higher profits. That's the way the competitive free
18 market works. So, it's absolutely right to understand that
19 American Express is motivated by profit. They should be.
20 That's what made this country great. They've got to keep
21 trying to do a good job, but it doesn't give them a free pass
22 from facing competition.

23 And so, this brings us, frankly, to their defense,
24 but before I do that, I want to go on to this next point which
25 is to note that Discover is another entity in this market that

1 is also a closed loop, they're an issuer, an acquirer and a
2 network. They don't share this inexorable up and down view
3 that is implicit in Amex's argument. You can see that here in
4 the testimony from Mr. Hochschild.

5 We asked him when you set your prices for merchants
6 for accepting Discover card, do you consider the reward? No.
7 If you increase the cost to your reward, in your view does it
8 justify telling a merchant that his price is higher? No. So,
9 there's another market participant that is similarly situated
10 in some ways to American Express that doesn't take this same
11 up one down the other point of view. So, it's not the only
12 way to look at the market.

13 So, what does this two-sidedness argument come down
14 to? In a way, it really comes down to we're entitled to
15 protection for our way of doing business. We heard this in a
16 couple forms in the course of the trial. The first form that
17 we heard it in was the suggestion that American Express would
18 go out of business if the anti-steering laws were removed.
19 Now, this was an argument that wasn't made in the answer or in
20 any expert report or in motion practice or I think even in
21 Amex's Pre-Trial brief or opening. It showed up during the
22 trial and frankly, the weight of the evidence did not support
23 that extreme form of its claim.

24 You remember Mr. Gilligan and maybe it was clear to
25 everybody in the courtroom than it might be on the cold

1 record, his response to the idea that American Express would
2 go out of business could probably be characterized as
3 disbelief. He said well, I plan to work here for another ten
4 years until I retire. Amex's testifying experts didn't
5 support the claim that Amex would go out of business. Amex
6 had an expert whose job was to talk about profitability. He
7 didn't come to trial.

8 In short, the evidence just didn't back up the claim
9 that Amex would go out of business if it didn't have
10 anti-steering rules. But if the Court will recall, you can't
11 really be too harsh on American Express for presenting this
12 because the claim that we're going to go out of business if we
13 have to face some new competition is something that's commonly
14 said by antitrust defendants who might be antitrust
15 defendants.

16 And the Court remembers the examples of the Visa
17 executive who testified in U.S. v. Visa that if the Court
18 ruled for the United States, Visa would disappear or the
19 MasterCard executive who testified that it would be a
20 shattered drawing put those into that same -- the statements
21 by American Express into that same category with those
22 statements.

23 THE COURT: Well, I, just as a surmise, I took that
24 comment by Mr. Chenault as not so much a definitive
25 conclusion, but as a statement of great concern that if the

1 Amex business model no longer had viability because of an
2 antitrust violation, that it would be a great challenge to a
3 corporation which rested its profitability on such a business
4 model to make adjustments and that that would be something
5 that could cause major changes. And so, uncertainties.

6 So, that's how I looked at it. And I think that's a
7 fair reading of it as opposed to we're just going to go out of
8 business. So, I understood it to be -- it was dramatic, but I
9 don't think it was meant to be absolutely definitive.

10 And I will ask Mr. Chesler about that, too. I'm
11 hoping he will agree with me. We will get there. We will get
12 there.

13 MR. CONRATH: I think that's a reasonable
14 interpretation.

15 THE COURT: So, I don't want to look at that in the
16 extreme, all right?

17 MR. CONRATH: And there is a softer version of that,
18 is the way I would put it, which is we need these rules to
19 protect our differentiated business model.

20 THE COURT: Mr. Conrath, could we take a short
21 break?

22 MR. CONRATH: That would be great, Your Honor.

23 THE COURT: Let's take a ten-minute break and then
24 you can resume.

25 (Recess taken.)

1 (In open court.)

2 (Judge NICHOLAS G. GARAUFGIS enters the courtroom.)

3 THE COURTROOM DEPUTY: All rise.

4 THE COURT: Please, be seated.

5 All right, just try to speak directly into
6 microphone, there are some microphone issues.

7 Thank you, you may proceed.

8 BY MR. CONRATH: (Continuing)

9 MR. CONRATH: All right.

10 Your Honor, what I hope to do now, I took advantage
11 of the break to look through and make sure I can efficiently
12 use my time. What I'd like to do is go back to a couple of
13 other issues and then, not forgetting where we were in that
14 discussion, but I think I can work that in better if I go back
15 and answer some of the other questions, including about the
16 market and get back to that. So, I'm not forgetting that, but
17 I'm going to try do that and streamline the presentation so we
18 can use the time efficiently.

19 THE COURT: Very well, go ahead.

20 MR. CONRATH: So, I am on slide 26.

21 So, we talked a little about market definition in
22 the context of two-sidedness. I just want to touch that
23 because that was also another important theme of American
24 Express.

25 The Court will recall that the other dispute in this

1 was all about debit and how to think about debit, so let's
2 remember that the Supreme Court has reminded us in Continental
3 and Brown Shoe that market definition isn't to be used to
4 obscure competition, but to recognize competition where, in
5 fact, competition exists.

6 The standard of market definition is reasonable
7 interchangeability. That's well-established. And under the
8 antitrust laws, they tell us a way to address reasonable
9 interchangeability and it's this, and I'm going to summarize a
10 lot of what the evidence is and what the legal principles are
11 on market definition.

12 What the Courts tell us to look at on the question
13 of what's in the market and what's not, what's reasonably
14 interchangeable and what's not, is to ask this question. If
15 the credit card networks all got together and raised the
16 prices to merchants, what could the merchant do about it? If
17 the answer is what the merchant could do is turn to some other
18 product and defeat the price increase, then that other product
19 belongs in the relevant market. So, if merchants could shift
20 to debit and defeat a price increase by credit card networks,
21 then debit's in the market. But if they could not, then debit
22 is not in the market.

23 There is a standard way of implementing this part
24 the reasonable interchangeability. It's the hypothetical
25 monopolist test. Professor Katz did it. He found the

1 relevant market that the Court has heard about.

2 American Express's economist recognized that that's
3 an appropriate way to define relevant markets.

4 Professor Bernheim even testified that only once before had he
5 ever offered an expert opinion on market definition without
6 using a hypothetical monopolist test, but the American Express
7 economist did not do it here.

8 Let's talk through the basic logic of how
9 Professor Katz defined market using the hypothetical
10 monopolist test.

11 We start by noting that merchant demand to accept
12 credit cards is derived from consumer demand. Now,
13 American Express articulates that same point, but they act as
14 if that's the end of the analysis instead of the beginning.
15 As a result, most of the American Express evidence on this
16 subject winds up asking the wrong question. They only asked
17 about cardholders and not about merchants. Remember, market
18 definition, reasonable interchangeability, hypothetical
19 monopolist test, they're all about what happens in response to
20 a small price exchange. If the hypothetical monopolist tries
21 to raise the price the merchants pay, then they make that
22 price increase stick.

23 Amex's answer to that is well, let's see if
24 cardholders could switch to debit. That's the wrong question,
25 why would cardholders switch to debit? They don't see the

1 price increases. Not only do they pay it -- at least not
2 directly -- they don't see it's there. The person who pays it
3 is the merchant. That's who we've got to ask about, that's
4 what Professor Katz did. As he explained, when you think
5 about that, the question you have to ask is could merchants
6 stop taking credit card and just rely on debit cards? If
7 they're really in the same market, if they're really good
8 substitutes, that ought to happen.

9 What merchants think about when they do that is what
10 would happen to me if I stopped taking credit cards? We know
11 the answer because we asked a lot of merchants whether that
12 was a realistic possibility, but the logic behind it is look
13 there's a core group of customers who want to use credit cards
14 or who need to use credit cards. If I, the merchant, don't
15 take credit cards, I'm going to lose a substantial chunk of
16 those core customers who want to pay with credit cards.
17 American Express recognizes this concept. You will remember
18 the testimony about compartmentalizing the spend.

19

20 (Continued on following page.)

21

22

23

24

25

1 MR. CONRATH: And we asked merchants -- I'm going to
2 skip over a lot of evidence in the interest of time here,
3 but -- we asked merchants, Could you drop credit cards? None
4 of those merchants came in and said that what AMEX's theory is
5 is correct. None of those Americans said, No, no, I don't
6 have to worry about credit cards. I could solve all my
7 problems with debits cards.

8 They all explained realistically to take credit
9 cards is an essential and important part of doing business.
10 Let's draw on the one that I remember, Mr. Bouchard from Sears
11 says, We sell a lot of refrigerators and stoves. A lot of
12 people need to pay for those over time. They need to use a
13 credit card. We don't take credit cards. We are not making
14 those sales. You multiply that over merchant after merchant
15 after merchant, their core customers, merchants can't drop
16 credit cards. A merchant cannot substitute debit card
17 acceptance for credit card acceptance.

18 The Court asked me to focus specifically about
19 Travel and Entertainment merchants. Let's talk about the
20 submarket, the price discrimination market.

21 We tried and Professor Katz talked about within the
22 broader credit card market, credit card services to merchants
23 market a relevant market, a submarket, for T&E merchants,
24 Professor Katz explained. And we cited the relevant law in
25 our papers, the proposition that we are applying here.

1 It's appropriate, if there's a group of customers
2 that can be targeted and are more vulnerable to a price
3 increase than the general market, to define a narrower market
4 and look at that and ask, Is this an area in which competition
5 could be harmed, higher prices could be imposed? Professor
6 Katz did the same analysis and concluded, Yes, this is an area
7 where competition could be harmed.

8 AMEX, I think, has three criticisms of that
9 analysis, and let's go through each one. The first one is the
10 question whether price discrimination is even possible.

11 The Court remembers a lot of testimony, I suspect,
12 from merchants who are paying widely different prices.
13 Merchants pay widely different prices. AMEX says, Well,
14 that's not enough. You have to ask prices compared to costs
15 in order to ask whether really it's price discrimination
16 that's going on. Well, let's look at that.

17 If we look at slide 40, which is a place with an
18 internal AMEX document where AMEX did exactly that. This
19 document is a presentation that was made to Ed Gilligan and
20 Bill Glenn. It's from the division of American Express that
21 deals with Travel and Entertainment Industries, TEI, and it
22 talks about the concept of industry-specific variable
23 contributions, which is basically revenues, minus costs, and
24 they calculate them for industry by industry.

25 You can see the conclusion they reach. It's right

1 in the middle there. It says "TEI" -- Travel and
2 Entertainment -- "has some of the highest industry-variable
3 contributions in Merchant Services U.S. what that tells you
4 is, there is price discrimination. Even when you think about
5 cost, they are getting a higher margin out of the Travel and
6 Entertainment Industries. That's price discrimination. It
7 happens. It is possible.

8 You can look at the exact numbers here. They are
9 redacted from the public versions. In the slide, you can just
10 compare the T&E variable-contribution margins for car rentals,
11 lodging and the others to the -- to the blue box with the
12 yellow below. Looking at the rest of Merchant Services U.S.,
13 you can see, yes, there is, even when you take costs into
14 account, there are higher prices for T&E. That first criticism
15 doesn't hold water when you look at the facts.

16 The second criticism American Express makes, they
17 accuse us of not defining the boundaries of the T&E market
18 precisely enough. There's plenty of evidence in the record on
19 this point.

20 The next document really just sums it all up. What
21 is T&E? It is a well established proposition. The previous
22 document was AMEX's own division for Travel and Entertainment.
23 This document is another document. It lists exactly the
24 categories that we're talking about when we talk about Travel
25 and Entertainment, and it even lists many of the largest

1 merchants, the managed merchants in those categories.

2 So what is T&E? It is well established in the
3 record. That's clear. That's not a valid criticism. The
4 final criticism they make is a little different. It's one
5 that I have never heard before. It is that no firm, they say,
6 could do business and sustain itself only in T&E. Well, that's
7 a little bit of a red herring. There's no authority that they
8 have cited for the proposition that a relevant market has to
9 be something in which a firm could sustain itself. They cite
10 no authority for that proposition, and for the well-known
11 reason that it's often the case that firms sustain themselves
12 by competing in a variety of different markets.

13 And the Court, I think, heard the testimony on one
14 of the most obvious examples of this, which is airlines, where
15 it's well established that the relevant markets in airline
16 industries are city pairs, so the competition between New York
17 and Houston is different than the competition between Chicago
18 and Dallas. And yet no firm could sustain and no airline
19 could sustain itself today serving just one of those relevant
20 markets; that is, New York to Houston or Chicago to Dallas.
21 Just to be an airline, you have to compete in a variety of
22 different markets. That's true.

23 That doesn't get in the way of answering the
24 relevant question from an antitrust perspective, which is, is
25 there a market where competition could be harmed? And the

1 answer to that in the airline industry is, Yes, for a city
2 pair. It is also yes in this industry for Travel and
3 Entertainment. Merchants within that sector are more
4 vulnerable, because they are more dependent on credit cards
5 and more dependent on American Express than merchants in other
6 sectors.

7 THE COURT: Is that really a fair analogy? In the
8 case of city pair comparison, first of all, in terms of
9 mergers, there's a lot of activity on the part of regulators,
10 including the Justice Department, in identifying potential
11 antitrust implications of proposed mergers.

12 In this situation, slide 41, you're talking about a
13 wide range of merchants, hundreds, thousands of merchants, and
14 you're not so particularized to two or three merchants
15 competing on a rarified basis between New York/Chicago or
16 San Francisco/Miami or whatever. Is there a difference if
17 you've got a wide range of merchants, as opposed to an
18 industry where there are very few competitors?

19 MR. CONRATH: So, I think maybe I should do a better
20 job of making the analogy. I think the answer is that the
21 comparison is appropriate. There are a few competitors in the
22 airline industry. Airlines are the sellers in the airline
23 markets. The buyers are diffuse. They are all of us who
24 travel. Those are the customers. So, the competition is
25 among the airlines to sell people who want to get from

1 New York to Houston. In the credit card space, there are few
2 networks competing with each other to do business with the
3 merchants who are in the Travel and Entertainment space, who
4 are the customers, and in this case take the place of the
5 individuals who travel.

6 So, the question is, If I'm a person who wants to
7 fly from New York to Houston, the relevant competition
8 question for me is, What are my competitive offers? If I'm a
9 merchant in the T&E space and I'm saying, I want to take
10 credit cards, what are the competitive offers that I've got?
11 Well, it's the same four that we know. I only have four.

12 And if I'm a merchant in the T&E space, I'm
13 particularly vulnerable, because a lot of people who want to
14 do business with T&E merchants are doing it with a corporate
15 card or a charge card, in which they really want to earn
16 rewards, so they are very insistent, more insistent than the
17 others.

18 I think the analogy is, in fact, right, and it talks
19 about how antitrust market definition and analysis works, and
20 this is why we often read about mergers that are resolved by
21 spinning off a particular asset that lets you compete in this
22 market.

23 So, the whole company was competing in a lot of
24 markets. There was a reduction of competition in one or two
25 of them, maybe a merchant monopoly in one market, and the

1 antitrust solution was, We'll analyze competition in that
2 market where there's a merger of monopoly. If the company
3 spins off that asset so the merger no longer turns it into a
4 monopoly there, we can solve it. You see, the company as a
5 whole is competing in a lot of different markets. They are
6 not asking the question, How do you sustain yourself just by
7 competing in that single market?

8 THE COURT: We also had testimony regarding
9 corporations who have arrangements with different credit card
10 issuers having to do with their corporate travel arrangements.
11 How did that fit in, inasmuch as a company, company X, company
12 X can choose to go to a bank where it does most of its
13 banking, like Wells Fargo, which has a Visa card that it
14 offers, and corporation X can require all its employees to
15 travel on the Visa card -- corporate card from Wells Fargo.
16 How does that fit into this T&E analysis?

17 MR. CONRATH: I think there might be three levels to
18 that answer. So, there are --

19 THE COURT: I'm sorry?

20 MR. CONRATH: I'm worried about my time, your Honor,
21 so I'm going to say it fast.

22 THE COURT: You have time. I told you I'm here
23 until 6:00.

24 MR. CONRATH: Thank you, your Honor. We'll try not
25 to abuse that.

1 THE COURT: Go ahead. I'm more interested in
2 understanding than about whether you meet your time
3 requirements or not. It's not carte blanche to do whatever
4 you want. Maybe that's the wrong term to use. I'm trying to
5 understand. So, if you can help me understand, that's the
6 objective here.

7 MR. CONRATH: I'll try to be helpful, your Honor.

8 THE COURT: Go ahead.

9 MR. CONRATH: So, there is a set of competition to
10 be the Cobrand cards for airlines, and, of course, you heard a
11 lot about that. That's competition that relates to the
12 issuing side.

13 So, AMEX and another, banker two, competed to be
14 Delta's Cobrand. They offered Delta various attractive
15 offers. Delta bid them against each other. The ultimate
16 upshot was that Delta helped AMEX issue cards. So, that's a
17 kind of competition that is related here. Doesn't go directly
18 to the merchant interaction.

19 There's another kind of competition -- this, I
20 think, is what your Honor was asking me about -- to be the
21 corporate card of a corporation. So, I'm Crate & Barrel. I
22 would want to have my employees have our corporate card to
23 travel with. I will solicit bids from the different credit
24 card networks -- issuers, rather, to be my -- to provide
25 corporate cards for my employees. That's a kind of

1 competition also where the corporation is going to choose one,
2 so it can get benefits of competition.

3 I think the court has heard that AMEX has a very
4 strong position in corporate cards. I think their internal
5 records say something like seventy percent spent on corporate
6 cards is on AMEX cards. But there are other operations for
7 the corporation in figuring out, Who do I want to be the card
8 that I will give to my employees? That's another area of
9 competition.

10 How that affects merchants, the question for
11 merchants is, What cards do I have to accept and what are the
12 prices and the conditions? What competition do I get as a
13 merchant among the credit card networks?

14 The way the corporate card thing works out -- works
15 is, a lot of corporations give it to you and say, Here, use
16 this when you travel. That makes that customer a very
17 insistent customer, from the perspective of the merchant. If
18 I'm the airline or the hotel, I need to accept American
19 Express cards, because there's so many American Express
20 corporate cards. So, that is one of the ways that that -- the
21 way that kind of competition showed up mainly in this trial,
22 is explaining why T&E merchants are so dependent on accepting
23 American Express even in the face of very substantial price
24 increases.

25 Now, what about -- there are two more pieces. I

1 think there are four instead of three. I think the two more
2 pieces are this: The Court also heard evidence about
3 corporations doing business with -- can a corporation do
4 business with -- choose to do business with a particular hotel
5 chain or a particular airline? So, here, the most interesting
6 evidence actually comes from a different part of AMEX, which
7 is the travel agency part.

8 Your Honor may recall, it's a small part. It used
9 to be a bigger part of AMEX just running travel agencies
10 mainly on behalf of corporations. You remember Mr. Corbett
11 came in, and what he testified to is that AMEX is effectively
12 in the role of American. AMEX is fine with steering. They
13 say, We will sign preferred deals with particular airlines,
14 and we'll steer our customers to those preferred airlines who
15 are paying us to be preferred. That's exactly what ought to
16 happen on a credit card space.

17 Merchants, just like AMEX does when it's a travel
18 agency, merchants ought to be free to sign a preferred deal,
19 get some compensation for that and encourage their customers
20 to use a particular card.

21 Now, one of the things that Mr. Corbett said is that
22 that doesn't always -- We can't steer everybody, because some
23 corporations have their own preference, and that's true. So,
24 a corporation might say, I've got a corporate preference. Not
25 the individual traveler, necessarily, but the corporation

1 prefers Hilton. We have a deal with Hilton, and those
2 travelers will go with Hilton. But from Hilton's perspective
3 as a merchant, the question -- I don't think that alters their
4 calculus on, Do I have to accept American Express? Do I have
5 to accept Visa? Do I have to accept MasterCard and Discover?
6 That's an example of what customers showing up at the door
7 want to pay with, those particular cards.

8 Maybe the final example on this topic, if you'll
9 remember, is a kind of steering that Mr. Thiel of Alaska
10 Airlines wanted to do and found that he couldn't do, which was
11 to approach some of the corporations that are in a city where
12 they could do a lot of travel on Alaska Airlines and say to
13 them, Hey, can I cut a special deal with you? If you steer
14 your customers -- if you'll send your customers to me, I can
15 make a separate arrangement to pay you.

16 He said he raised that -- so, that's a form of
17 steering, a form of competition. Mr. Thiel wants to say, If I
18 can get you to do business with me directly, I can do more
19 business. He said he raised that with American Express, and
20 the answer -- I wish I can remember the exact phrase -- he
21 said, The answer was immediate and negative. You can't do
22 that kind of steering.

23 That's -- so, that kind of arrangement that a
24 merchant might want to do with -- that a merchant, Alaska,
25 might want to do with some of its customers, business

1 travelers, is blocked by the antisteering.

2 So, I think those are the ways in which that kind of
3 corporate relationship with travel merchants and with the
4 networks plays out.

5 Have I answered that enough? Okay.

6 So I, guess where we are is, on the T&E market,
7 defining a submarket or price discrimination market like that
8 is a well accepted form of market definition. The market for
9 T&E merchants meets all the relevant tests, and the defenses
10 that we heard from the other side aren't enough reason to tell
11 us that we ought to take that off the table. So, that's a
12 legitimate form of market definition that should be considered
13 by the Court.

14 I would like to talk briefly about market power. If
15 we could go to slide 44. The Court will remember this. This
16 is a slide we put up at the beginning of the trial.

17 I just want to say -- we told you what we were
18 planning to prove. I would like to briefly note this proof
19 came in. This is a roadmap. The U.S. v. Visa laid out a
20 roadmap for how to analyze market power. A lot of times, the
21 court doesn't have the benefit of having this kind of a
22 roadmap.

23 We have gone through and proved these elements. The
24 anti-competitive effect I have already talked about. That was
25 one of the ways the U.S. v. Visa court concluded there was

1 market power.

2 Customer insistence. American Express is very
3 clear, in both what it does internally and what it tells to
4 its merchants, that they have a lot of insistent customers.
5 The Court of Appeals told us, in USA v. Visa, that's a fact
6 for the judge in evaluating whether they have market power.
7 AMEX tried to say this is just puffery or salesmanship. The
8 record evidence shows it's something they track very
9 carefully. They quantify and use it in making decisions.
10 They use it in explaining to merchants why they ought to pay
11 the higher prices that American Express charges.

12 The third category of evidence on this roadmap is
13 price increases without losing merchants. We went through the
14 example of value recapture, where American Express raised
15 prices on merchants representing sixty-five percent of its
16 travel volume. No large merchants lost negligible, small
17 merchants lost negligible suppression. The evidence
18 established this element of the USA v. Visa roadmap, as well.

19 THE COURT: But on value recapture, wasn't that
20 overall kind of an unsuccessful program for American Express?
21 So, in spite of everything, the -- and all the arguments with
22 customer insistence and other arguments made with regard to
23 customers, and it still was not a successful program.

24 MR. CONRATH: They had a couple of points about
25 that. Frankly, they are not supported in the evidence. Let

1 me go through those points.

2 MR. CONRATH: If we look at slide 49. This is
3 American Express's sum-up of where they were on value
4 recapture as of 2010. What is the global cumulative benefit
5 of the value recapture program? And you can see, these are
6 the five years, and as the Court recalls, it ended after this
7 case was brought.

8 THE COURT: I'm sorry. Is this a public document?

9 MR. CONRATH: There are a couple of small
10 redactions. I believe we have all the redactions that are
11 required.

12 MR. CHESLER: There are redactions, your Honor.

13 THE COURT: That's fine. Thank you.

14 MR. CONRATH: Thank you, your Honor.

15 The way this works, 2006, they imposed the price
16 increases that are reflected in blue, and they increased that
17 amount of PTI or Pre-Tax Income as a result of the price
18 increases, and those same price increases you can see
19 continued over the subsequent years.

20 Then there's another set of price increases in 2007.
21 That's the green price increases -- the red, by the way, is
22 international. So, the rest of this is domestic. I'm going
23 to ignore the rest -- and the green price increases, they
24 continued to be in effect over the next years. Then in 2008,
25 an additional set, 2009, and the projections for 2010.

1 What they summarize, this has brought us a net at
2 this point of \$1.3 billion. Of course, I heard that they
3 didn't add additional new price increases after 2010. But as
4 you can see with what happened with the blue bar and the green
5 bar here, those price increases continued to be in effect in
6 the market.

7 The Court will recall the airlines who came in who
8 experienced substantial price increases, and they said they
9 are still paying them. Those weren't rolled back. So, those
10 were successful price increases implemented in a market, made
11 money for American Express. American Express says, No, no, it
12 was not successful. They say a couple of things about that.
13 Let me touch on each of them.

14 THE COURT: They discuss the rewards program in the
15 context of that, don't they?

16 MR. CONRATH: So, they discussed the rewards. I
17 think there are three topics. One is the rewards program, one
18 is their claim that it backfired, and one is their claim that
19 overall, our prices were going down. Let me touch each one of
20 them in turn.

21 THE COURT: Go ahead.

22 MR. CONRATH: So, the claims about the reward
23 program were claims made by Professor Bernheim that -- and his
24 claim was, did -- his claim was that the cost, American
25 Express's cost of its reward program, went up so much that it

1 negated some of the benefit of the price increase to
2 merchants.

3 So, Professor Katz had looked at that and said there
4 isn't evidence in the record, and he said the evidence doesn't
5 establish that they were raising the prices, and it was all
6 disappearing into rewards. He said, No, it was profitable.
7 He looked specifically at the claims made by Professor
8 Bernheim. He found a series of mistakes in there. The
9 fundamental mistake is, he's asking what the rewards program
10 cost American Express, not, What is it worth to the
11 cardholder?

12 So, if the claim is that there are benefits to the
13 cardholder, that's not asking the right question. Some of the
14 specifics we looked at illustrated that. So, for example,
15 there was a period when Continental withdrew from the American
16 Express program, the value recapture program. That made the
17 value recapture program less valuable to cardholders. It's a
18 diminution in value.

19 How did Professor Bernheim throw this into his
20 numbers? He looked at what happened in the short run, which
21 was, a lot of people who had American Express miles and lived
22 probably in Houston thought, I want to use these miles
23 immediately, before I lose the chance to use them on
24 Continental. So, there's a big bump-up in the cost to
25 American Express as people rushed to use their miles, because

1 they didn't have the option. The miles were worthless if they
2 did not use them. They were not going to be able to use them
3 on Continental. They rushed to use them. That ran the cost
4 up, even though what really happened was, the value of the
5 program went down.

6 We saw the same thing. Professor Katz went through
7 and analyzed this with respect to Delta. Delta finds itself
8 in the position that it was in, whatever, made decisions to
9 make the value of the Sky Miles less, to diminish the value of
10 the Sky Miles. It's harder to find a flight. You have to pay
11 more miles for a flight. In various ways, you know, acting as
12 appropriately in their own interest of protecting their own
13 profits, it made the Sky Miles program less attractive to
14 cardholders. That's a diminution of value to the cardholders.

15 At the same time, American Express has to buy Delta
16 miles from Delta, so that they can give them out in their
17 rewards program, but because Delta was in a position to do so,
18 it raised the price to American Express of the Sky Miles. And
19 so, Professor Bernheim said, Oh, look, American Express is
20 paying more for Sky Miles. I will add that to the cardholder
21 benefits, and implicitly assume that's good for cardholders,
22 when in fact for the same number of miles, American Express
23 was paying more, but cardholders were getting less, because
24 Delta was now in a position to deliver less.

25 So, it's another way in which Professor Bernheim's

1 calculation, looking at how much does the rewards program cost
2 American Express, was asking the wrong question and coming to
3 a wrong conclusion.

4 So, Professor Katz's analysis was, there was a net
5 increase, even if you think of it two-sidedly, because
6 American Express was able to raise prices in value recapture,
7 and there were not offsetting rewards increases.

8 Professor Bernheim made a responsive claim that
9 actually there was an increase, but he measured the wrong
10 thing. What he said was, there was an increase in the cost to
11 American Express.

12 Professor Katz looked at that and said, Not so. You
13 look at what's really going on here, it's not an increase in
14 the value to the cardholders, it's not a benefit to the
15 cardholders, it's a higher cost to American Express, but not a
16 benefit to cardholders. That doesn't reverse my conclusion
17 that value recapture was a profitable price increase, where
18 AMEX didn't lose merchants, because they have market power.

19 The final way in which American Express tries to say
20 this was not profitable or wasn't successful is, they say it
21 backfired. They say, We annoyed our merchants. You probably
22 heard that some of the merchants were annoyed by these price
23 increases. You also heard the evidence that they could not do
24 anything about it.

25 There's one example that American Express points to,

1 and that's Continental. What they argue, and they continue it
2 in their brief even though it's contrary to the evidence, is
3 to say that Continental was so angry at the price increase --
4 and it is true Continental was angry at the price increase,
5 there's no dispute there. They say that is what caused
6 Continental to pull out of making its airport lounges
7 available to American Express card members as part of its
8 membership's part of the cardholder benefit and pull out of
9 the rewards program, letting people use their rewards on
10 Continental.

11 The problem with that is that the contemporaneous
12 evidence just doesn't support the claim that there was
13 retaliation for the price increase. The contemporaneous
14 evidence includes, my recollection is, two documents. One is
15 a document from the president or maybe the chief operating
16 officer of Continental, saying, The reason we have to do this
17 is that we've got a Cobrand with Chase, I think, and we
18 couldn't continue to have -- to be in the AMEX reward program
19 under our Cobrand agreement, or we would have to pay Chase
20 huge penalties. That was going to happen no matter what.

21 And a contemporaneous American Express document
22 reports that same fact, says, The reason Continental is
23 pulling out is because their deal with Chase, their Cobrand
24 deal with Chase, requires it.

25 The argument that we are hearing in AMEX's papers,

1 that Continental punished us by pulling out of the rewards
2 program and pulling out of the lounge program because of our
3 value recapture price increase, is just not supported by the
4 record evidence.

5 THE COURT: Continental could have negotiated a deal
6 with Chase that accommodated American Express cardholders with
7 regard to the lounge situation. They could have leased space
8 at Newark Airport to American Express to create its own
9 lounge. They have space at Newark terminal, wherever they are
10 at over there, that they had total control over.

11 And so, it may be that the primary reason was that
12 -- for the change, that it now had a Cobrand relationship with
13 Chase. But it didn't have to exclude American Express card
14 members who buy tickets on Continental Airlines, I'm sure,
15 notwithstanding the fact that they are not the Cobrand card
16 for Continental. They could have made adjustments,
17 accommodations so as not to inconvenience their own customers.

18 So, there must be -- my surmise is that there may be
19 some truth to the fact that they were not only not going out
20 of their way, but there might have been a form of retaliation.
21 You don't know that it wasn't or that it was. You just know
22 that there's a Cobrand agreement with Chase, and that many of
23 the aspects of what would have been a Cobrand relationship
24 with American Express are now reposed in that relationship
25 with Chase; isn't that right?

1 MR. CONRATH: Respectfully, I don't think so, your
2 Honor, and let me tell you why.

3 THE COURT: Is there anything in the record about
4 that one way or the other? That's the question, I suppose,
5 and not my imagination about the aviation industry.

6 MR. CONRATH: Let me address both the aviation
7 industry and what's in the record. What's in the record is, I
8 believe, two documents.

9 One is from a very high official at Continental
10 saying the reason -- he does indeed express frustration with
11 the price increase, no denying that, and lots of merchants who
12 came here did, saying The reason we have to do this is because
13 of our deal with Chase.

14 And there is a contemporaneous document from
15 American Express at that time repeating that statement. This
16 was -- I don't know if the word "baked in" is used. That's
17 the idea. This was going to happen.

18 Now, but let's just think about this logically.
19 Could they have negotiated something? Well, maybe. We don't
20 know. There is not record evidence about what they could have
21 negotiated.

22 THE COURT: They have a lot of tenants over in that
23 terminal with whom they don't have a Cobrand agreement.

24 MR. CONRATH: Sure.

25 THE COURT: For instance, you know, they probably

1 have all -- all those places you go to eat that you shouldn't
2 go to eat; right, when you're getting on an airplane, or at
3 any other time, for that matter? All right.

4 MR. CONRATH: I think, in fact I believe that is
5 what's happening in that market. American Express has leased
6 some space in a few airports, and I don't know if Newark is
7 one of them, but they have leased some space in a few airports
8 to set up their own lounge called the Centurion Lounge, in
9 part because as markets were changing, they found that not
10 just Continental but I think other airlines were not willing
11 to renew the prior arrangements they had. And so, in some
12 places, American Express is leasing a space, and they are able
13 to find it, whether from an airline or from an airport
14 authority, and setting up their own lounges in order to
15 provide this benefit.

16 But I think the way to think about this market,
17 though, the relationship with Chase -- I hope I'm remembering.
18 I believe it was Chase. It was a bank. We'll talk about
19 Chase. I think it's right.

20 Chase and Continental negotiated the terms of that
21 agreement. Presumably -- I mean, just as you say thinking
22 about the incentives, Continental is giving up something by
23 promising not to have to do something with other airlines.
24 So, Continental is giving something up in order to make these
25 promises to Chase. Presumably, it's part of the whole

1 bargain.

2 Chase thinks it's worth it to them, and Continental
3 finds the total package worth it to them. So, it's not like
4 -- and there's certainly not any record evidence to suggest
5 that Continental could have just gone to Chase and said, Hey,
6 why don't you drop this provision of the contract? No reason
7 to think that that's right, because Chase was getting
8 something for it, and we don't know.

9 But maybe what they are getting is, you know, access
10 that they can use to sell to their potential cardholders,
11 access and maybe exclusive access at particular airports, and
12 that's how competition works.

13 And the most important thing is, though, what it
14 says is that the decision that Continental made to cancel the
15 participation with American Express was driven by this
16 relationship with Chase. Whatever else they negotiated or
17 could have negotiated with Chase, that's not -- the evidence
18 is clear that is what was driving their decision to terminate
19 that relationship. They said, We would have to pay -- I think
20 the phrase is, We would have to pay some amount of money in
21 penalties to Chase if we didn't go ahead and do this. So,
22 that tells you there's a contractual arrangement that the two
23 parties negotiated and that made sense for them.

24 So, this only comes up in our case, because American
25 Express raises it. We kind -- how airport lounges get

1 resolved is kind of far afield. It only comes here because
2 American Express makes the claim, which is just wrong, that
3 the reason for that change was that Continental was
4 retaliating for that particular price increase. The evidence
5 just doesn't support that.

6 I guess I should, while I'm at it, point out the
7 other little thing that's wrong with the argument they are
8 making. They are comparing in that -- the analysis that's in
9 the brief compares one point something billion in charge
10 volume, and compares that to the one point three billion in
11 Pre-Tax Income that was from the value recapture. That is a
12 huge apples and oranges comparison.

13 Charge volume is the whole price of the airline
14 ticket. The income that American Express gets out of that is
15 a couple of percent. So, even when they are making -- the
16 argument is wrong as a factual causation matter. But if you
17 look at what's being argued there, the comparisons that they
18 are making to try to over dramatically say, This wiped out any
19 benefit of the value recapture program, they are not even
20 comparing apples and oranges. They are comparing apples and
21 bicycles, frankly. Just this whole argument from American
22 Express just does not hold water.

23 Finally, you asked me about one other part of
24 American Express's argument about whether they were able to
25 increase prices. They claim, Look, no, our prices really went

1 down. They use some arguments from Professor Bernheim on
2 this.

3 I'm going to switch to slide 52. There are two
4 things that Professor Bernheim did wrong that let him say
5 prices are going down instead of up during the value recapture
6 period. One is, he ignored mix. Part of what was going on
7 was that as AMEX did less business at the expensive Travel and
8 Entertainment merchants, and a higher proportion of its
9 business at the cheaper, everyday spending business, their
10 average price would, of course, go down even if all the prices
11 are staying the same or even increasing. So, he missed the
12 mix adjustment.

13 The other thing was, he made some frankly remarkable
14 changes to the discount rate revenue.

15 And if you look at the next slide, 53, this is a
16 slide from Professor Bernheim's report that we used in the
17 trial. The Court may recall -- you can see here, this is
18 prices to the major domestic airlines, the largest airlines.
19 You'll see that virtually every domestic airline, you can see
20 the effect of the value recapture price increase on this
21 chart.

22 If you look at the price in the earliest year and
23 the price in the latest year, it's a pretty substantial run-up
24 in price, with two exceptions, JetBlue and Delta, and those
25 are two airlines that have a Cobrand agreement with American

1 Express.

2 What Professor Bernheim did was, he took all the
3 revenue from the Cobrand agreement, which is, he talked about
4 before, is an issuing-side agreement related to Delta getting
5 in the hands of a lot of people some American Express cards.
6 He took all that revenue, and he put it into this assessment
7 of what is American Express's revenue from its merchant
8 acceptance fees. That produces the remarkable and, frankly,
9 incredible result that all the airlines in the country are
10 paying American Express several percent for the privilege of
11 accepting the American Express card.

12 But Delta is exactly the opposite. He says with
13 Delta, American Express is paying Delta for the privilege of
14 having American Express cards there.

15 As Professor Katz says, that just economically makes
16 no sense. The implication is that all the Cobrand payments
17 are a net zero, because he counts all the Cobrand revenue and
18 the pre-payment of miles revenue in as discount revenue.

19 If you want to know how important -- we know,
20 because there was testimony, that the reason Delta got a good
21 deal in that Cobrand in that prepurchase of miles negotiation
22 was, there was competition to be the Cobrand partner,
23 competition between American Express and one or two other
24 banks.

25 The suggestion that that -- that's why there are

1 these huge payments to Delta under the Cobrand and the
2 prepurchase agreements. It's not because Delta agreed to
3 accept the American Express card. It was going to accept the
4 American Express card whether or not it was the Cobrand deal,
5 and it would be paying a price probably along the line of what
6 the other airlines are paying. The idea that every merchant
7 in the country is paying American Express but in this one case
8 it's the other way around just frankly is incredible.

9 The effect of this, we see on the charts that are on
10 the next page. You can see the left-hand upper chart is
11 general markets. The lower one is T&E. I'm just going to talk
12 about the general markets.

13 Professor Bernheim's calculation -- this is what
14 leads Professor Bernheim to say prices go down -- is the black
15 dashed line at the bottom. Professor Katz said, If we just
16 correct for the Jet Blue and Delta errors, what we did is the
17 blue line in the middle. So, you can see how huge is the
18 effect of that particular choice that Professor Bernheim made.
19 If we also correct for mix, you can see the orange line at the
20 top, which shows, as we've talked about, prices are going up
21 during the relevant value recapture period.

22 I think I was going through U.S. v. Visa roadmap
23 saying, We proved all the evidence we said we were going to
24 prove. I'll gloss over the last one, which is market share,
25 and there's no dispute about the barriers to entry here.

1 In U.S. v. Visa, the Court found that MasterCard,
2 which was the number two firm at that time, had market power
3 with a twenty-six percent share. Today, American Express is
4 the number two player in the industry. It has a twenty-six
5 percent share. AMEX agreed, when it sued MasterCard, the
6 twenty-six percent share was part of having the market power.
7 AMEX today has that. That's another element in the proof that
8 we have met.

9 The Court asked about T&E. I'm going to skip some
10 other slides about the market power. It's well established.

11 Because the Court asked about T&E, I would like to
12 talk about slide 59, which tells us that American Express's
13 market power is even more apparent in the market for Travel
14 and Entertainment merchants. All the same market powers in
15 the U.S. v. Visa are here and even more so. The market for
16 T&E is 34 percent. Spend coverage is higher here than the
17 already high number that it is elsewhere. Insistence is
18 stronger for T&E merchants than it is for the general market,
19 primarily because of corporate card insistence. Also, if you
20 look at the way AMEX calculates, the insistence for T&E
21 merchants is higher.

22 On value recapture, the question of whether you can
23 impose price increases without losing customers, American
24 Express has special campaigns for raising prices in T&E
25 industries. The Court heard evidence from a number of

1 airlines on the price increases that they faced. It also
2 might remember evidence about restaurant value recapture one,
3 two and three. So, the price increase evidence is even
4 stronger in the T&E industry than it is in the other. And in
5 the same vein, you recall the margin evidence, the
6 variable-contribution evidence from the slide that we looked
7 at a little bit before, that shows that AMEX takes in more
8 revenue compared to costs in the T&E industries than it does
9 in other industries. All of these just tell us that the
10 market power evidence that establishes generally that American
11 Express has market power is even stronger for the T&E sector.

12 (Continued on next page.)
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1 MR. CONRATH: (Continuing) I've got just two more
2 topics I want to talk about, Your Honor.

3 When faced with this evidence, what does American
4 Express say? I think I've got two things left I want to talk
5 about. One is welcome acceptance.

6 They say we need to have these restrictions in order
7 to guarantee welcome acceptance at merchants, welcome
8 acceptance of the American Express card.

9 Well, this claim has been a little bit of a moving
10 target. The Court may recall that before trial, what American
11 Express said was we need the rules in order to prevent
12 embarrassment of the cardholders when they try to use their
13 American Express card.

14 At trial, as indicated in the slide I'm looking at,
15 slide 62, at trial, they walked away from the embarrassment
16 claim. And also at trial, the Court may recall that we asked
17 various American Express witnesses examples where steering is
18 allowed or takes place and said, well, does that interfere
19 with welcome acceptance, and they said no. And this is no
20 surprise because merchants testified about steering and they
21 said, look, if we have the freedom to steer, we will do
22 steering in a way that keeps our customers happy for the very
23 good reason that they want that customer to come back.

24 John Robinson of IKEA was just one of many merchants
25 who testified to that.

1 Are you able to engage in these promotions without
2 annoying or offending your customers?

3 Yes.

4 And is that important to you?

5 Yes.

6 Well, naturally it is. They want the merchant to
7 come back.

8 The other reason why we, we know this welcome
9 acceptance argument is wrong on the facts, just on the facts,
10 is that AMEX itself steers when it feels like it's in its own
11 interest to do so.

12 So we talked a moment ago about how AMEX steers in
13 its travel agency. And Mr. Corbett testified that they're
14 able to do that without annoying or offending the customers.
15 AMEX has used prompting at checkout at merchants that have
16 AMEX co-brand cards without causing unwelcome acceptance.
17 There are discounts available only if you use AMEX at
18 Universal Studios I talked about with Mr. Chenault. No
19 unwelcome feeling for other credit cards there. The
20 preference arrangements AMEX has had with various other
21 entities without causing or any evidence that that causes
22 unwelcome acceptance.

23 The Court will remember Mr. Glass's signs. This is
24 one of them, that AMEX said would be prohibited. The
25 anti-steering rules wouldn't let them, wouldn't let a merchant

1 put up a sign that said this checkout line is for Discover
2 customers only. And guess what? We found out during the
3 course of this trial that AMEX itself had exactly that deal
4 with Radio City Music Hall, a separate payment window for
5 American Express cardholders. They even had a provision in
6 the contract that if things got busy, somebody had to go out
7 in the lobby and say, hey, there's a special window over here
8 for American Express Cardholders only.

9 So you can't just take seriously as a factual matter
10 this claim that steering somehow is inherently going to make
11 customers feel unwelcome. What really is going on here is
12 that American Express has taken the term "welcome acceptance"
13 and it's redefined it to mean something else basically.

14 They define "welcome acceptance" to mean, they say
15 we mean by that is there are no competitive offers from our
16 rivals allowed at the point of sale. Even simple truthful
17 pricing information can't be provided at the point of sale.
18 Well, look, if you can do that, if you can take a perfectly
19 neutral term like "welcome acceptance" and redefine it as I
20 don't have to face competition, lots of companies, and get
21 away with it under the antitrust laws, lots of companies would
22 sign up for that, but the law, the law doesn't allow it.

23 A defendant, as the court, the Supreme Court said in
24 National Society of Professional Engineers, a defendant cannot
25 impose its views of the costs and benefits of competition in

1 the marketplace. American Express can't say we won't allow
2 our rivals to compete with us in this way. That's just not an
3 appropriate antitrust response. You can't bootstrap yourself
4 into a legitimate pro-competitive justification for your rules
5 by defining no competition as welcome acceptance. They can't
6 cite any case authority suggesting that would be an
7 appropriate reason for a restriction on competition.

8 And they frame this a little differently and this is
9 the topic that we left on before the break, Your Honor, which
10 is they say we need these rules to protect our differentiated
11 business model. It's really an argument for protectionism and
12 it's well established in the antitrust laws that the antitrust
13 laws don't protect competitors that protect competition. They
14 protect the process.

15 The antitrust laws do not allow American Express to
16 decide what competition it will face and what it will not
17 face. Now, it's not surprising that AMEX, if it can get away
18 with it, would prefer to channel all the competition in the
19 market into the kind of a competition that American Express
20 likes, competition that provides the cardholder benefits, and
21 away from, to exclude the competition that American Express
22 does not like, competition to provide good value and low
23 prices to merchants.

24 That kind of argument was made in the second case
25 that I cited earlier which is Brown University. The

1 defendants argued there that there was a restriction on price
2 and the defendant said, well, okay, this restriction on price
3 just makes us compete harder on some other things. And the
4 court said, no, no, that is not a pro-competitive virtue.
5 That is a consequence of deciding not to compete on price.
6 You can't use that as a justification for your restriction on
7 price competition.

8 So it is, it is true, this differentiated business
9 model. It is true that it is good for competition for AMEX to
10 have the right to try its business model in the market. We
11 went to court 15 years ago to defend that right to try. That
12 does not mean that AMEX has a right to succeed to guarantee
13 its success by blocking competition from other rivals.

14 Now, AMEX cites a series of statements from the
15 United States in United States versus Visa talking about the
16 importance of AMEX having a chance to bring its model,
17 differentiated business model in the market. What's
18 interesting is each one of those also mentions Discover and
19 its differentiated model. And what about Discover? Because
20 if it's right that AMEX has a chance to try its differentiated
21 business model, so too does any other competitor have a chance
22 to try its differentiated business model. What about
23 Discover's differentiated business model?

24 Discover's differentiated business model was we'll
25 bring low prices to merchants, attractive innovative rewards

1 to cardholders. By the way, you can see it's a two-sided
2 innovative differentiated business model. That was squelched.
3 It was squelched by the anti-steering rules. It's still
4 squelched today as you heard the testimony from
5 Mr. Hochschild.

6 What does AMEX say about that? Well, I put that
7 question to Mr. Bernheim. His answer to Discover was
8 basically, well, why don't you try to be more like AMEX, why
9 don't you try to offer more rewards directly to cardholders.
10 That's not what the antitrust laws are about. You as a
11 competitor don't get to dictate how your rivals compete with
12 you. What the law requires is much simpler. Just let
13 different business models compete in the marketplace without
14 these extraneous restrictions on somebody else's competition.

15 If there's merchant demand and cardholder demand for
16 another model -- American Express says it does and there's a
17 lot of reason to think they're right, there's something good
18 for merchants, something good for cardholders -- if they're
19 delivering value to merchants and to cardholders together, the
20 market will let them find a way to do it. If they have to
21 adapt their model, they may have to cut their price a little
22 bit, that's what the antitrust laws require.

23 That package of benefits that they offer, if it's
24 got value and can succeed, it needs to do that in a world in
25 which other rivals are free to compete in their own

1 differentiated business model.

2 And what would happen if we get rid of American
3 Express's anti-steering rules? Really, the best answer came
4 from an American Express executive, Mr. Funda.

5 He says, If we didn't have these anti-steering
6 rules, we would be fighting to retain the business by any
7 means necessary, right?

8 He said, Yes, we may need to increase incentives to
9 consumers, we may need to increase pricing to merchants.

10 In other words, get rid of the anti-steering rules,
11 there will be more competition. That's what the antitrust
12 laws are all about. That's why these anti-steering rules are
13 a violation of Section 1 and I'm going to ask the Court to
14 find that and we hope that you'll see it our way.

15 Thank you, Your Honor.

16 THE COURT: Thank you very much.

17 Mr. Gentile?

18 MR. GENTILE: May it please the Court, Mitch Gentile
19 on behalf of the plaintiff States. Your Honor, I will be very
20 brief, just several minutes with respect to my argument.

21 We believe that the evidence elicited at trial has
22 shown that AMEX's anti-steering rules unreasonably restrict
23 price competition by limiting a merchant's ability to steer or
24 credit or charge transactions at the cheapest network.

25 The evidence has also demonstrated that AMEX's rules

1 even prevent truthful information concerning the cost of a
2 transaction from being disclosed by the merchants to their
3 customers as well as denying consumers the opportunity to
4 receive immediate benefits from a merchant based on a customer
5 selection of a lower cost credit or charge card.

6 AMEX's restrictions keep customers in the dark while
7 denying merchants critical tools for bargaining the credit
8 charge card networks. Thus, they restrain competition between
9 all the credit and charge card networks on the merchant side
10 of this market.

11 Credit and charge card swipe fees imposed by the
12 network merchants exceed over \$50 billion annually in the
13 United States. Those transaction costs incurred by the
14 merchants are then passed on by the merchants to all consumers
15 in the form of higher prices for products. What this means is
16 customers who pay with cash or that the poor who do not
17 qualify for credit cards are paying higher costs for their
18 products and services so that AMEX Cardmembers can receive the
19 rewards. When costs facing businesses are insulated from
20 meaningful competitive forces allowing them to be inflated
21 unilaterally, as has been demonstrated in this case, this is a
22 concern for all who enforce our competition laws. That is why
23 more than a third of the States have joined this important
24 litigation.

25 In conclusion, Your Honor, we urge this Court to

1 find that American Express has violated Section 1 of the
2 Sherman Act by its enactment and illegal enforcement of the
3 anti-steering rules.

4 Your Honor, on behalf of the seventeen plaintiff
5 States, we appreciate the time and the effort that you spent
6 on this litigation and we thank you.

7 THE COURT: Thank you very much.

8 All right. What we will do is take a lunch break
9 until 2:00 p.m. and we will resume with the defense
10 presentation at that time.

11 (Luncheon recess.)

12 (Continued on next page.)

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AFTERNOON SESSION

(The following occurred in open court.)

THE COURT: Okay. Yes, sir.

MR. CONRATH: One more thing, if I can approach.

We used one slide electronically because my
colleagues officially put it up that wasn't in the deck. We
already provided it to American Express. If I can make copies
available.

THE COURT: Just give it to Mr. Reccoppa. And your
slide presentation will be marked as Plaintiffs' Exhibit A.

MR. CONRATH: I think we haven't used that one yet.

THE COURT: This is A.

MR. CONRATH: And this is perhaps A-1, the one sheet
I handed you?

THE COURT: Very good. Okay. Thank you.

All right. Now we will proceed with the defense
closing.

Mr. Chesler?

MR. CHESLER: Thank you, Your Honor. Your Honor, we
too have some slides if we may hand them around.

THE COURT: That's fine. I was considering
prohibiting blue paper and to see if that might truncate your
presentation but it's too late now. It looks like the
Manhattan directory in blue.

MR. CHESLER: Your Honor has obviously not seen the

1 blue paper section of the due process clause.

2 THE COURT: That's right.

3 MR. CHESLER: If I may, Your Honor.

4 THE COURT: Please.

5 MR. CHESLER: Thank you.

6 I want to begin where Mr. Conrath began. His first
7 sentence, I believe, was that this market is broken and I'm
8 sure Your Honor won't be surprised to hear me say that it is
9 far from broken.

10 This is, in many respects, a case about two cases.
11 The parties look at largely the same facts and see them in
12 dramatically different ways and, frankly, I say with respect,
13 the government largely ignores large portions of the case and
14 I'm going to try to spend some time pointing out the more
15 important things that they ignored today and in their papers
16 and, frankly, during the entire trial.

17 It is a market, however, in which if the government
18 were to have its way, we believe it would be broken. And,
19 Your Honor, just as one tiny tidbit, Your Honor mentioned
20 PayPal this morning. News has just recently come out that a
21 man by the name of Dan Schulman, who is a very senior
22 executive in American Express, in fact, was deposed in this
23 case, is leaving to become the CEO of PayPal and it's part of
24 what Your Honor I think was talking about, about the evolving
25 nature of this market and things that the government discounts

1 because they don't fit their model, in fact, are quite
2 important.

3 Fourteen years ago, when the government called
4 Mr. Chenault to the stand as their principal witness in the
5 exclusionary rules case, as he testified under oath, the
6 Assistant Attorney General of the United States at that time
7 asked him to make sure that he emphasized the critical role
8 that the AMEX differentiated product model plays in the
9 marketplace, not to protect American Express, and indeed the
10 government never said to Judge Jones that they had brought
11 that lawsuit to protect American Express or Discover. They
12 said they brought it to protect competition.

13 The principal way in which they sought to prove
14 that, and it's all over the papers that are admissions of the
15 government and it's all over the record in that case and it's
16 all over Mr. Chenault's testimony about which he testified
17 here as well, was that American Express was the best hope in
18 the marketplace to deal with the dominant Visa and MasterCard
19 networks and without American Express and its differentiated
20 model, no company with the tiny share of cards in force, the
21 tiny share of spend volume, the tiny share as compared to the
22 others of issuing banks, et cetera, could hope to be a
23 successful competitor and that was critical to the well-being
24 of the marketplace.

25 Now, when that lawsuit was brought, American Express

1 had precisely the same nondiscrimination provisions in its
2 merchant agreements as it has now. It was actively enforcing
3 them in the wake of the We Prefer campaign that Visa had
4 perpetrated and I'm going to come back to that subject a
5 little later. It had something it does not have today which
6 is a premium over Visa and MasterCard on merchant discount
7 rates when you look at the average rate with proper mix
8 adjustment and we'll come back to that. And it has today the
9 same, almost exactly the same market share of consumer spend,
10 of customer spend as it had 25 years ago even if you leave
11 debit out of the market, which we believe would be incorrect.

12 So the only thing I would submit, Your Honor, that's
13 changed since that lawsuit was brought, and the government
14 made all of the admissions it made to which Mr. Conrath only
15 referred for a brief moment at the end of his comments, the
16 only thing that's changed is the position of the United States
17 Department of Justice. The same model has gone from being
18 pro-competitive to being a Sherman Act Section 1 violation.
19 They can't answer what they said before and they don't even
20 try because there is no rationale acceptable answer for that
21 turnaround.

22 As I said to Your Honor in the opening, the
23 government's case is premised entirely on guesswork, on
24 speculation. Our defense is based upon the facts. The
25 biggest speculation in which they engage, and it is remarkable

1 that an hour and 40 minutes of today's comments were about
2 competitive effects, and not once did the government mention
3 their principal witness on competitive effects with respect to
4 that issue, Dr. Katz, and there's a reason. Because Dr. Katz
5 on cross-examination conceded the government's case away.

6 The government must prove, as I'll come to in a
7 moment, if they don't move the goal post in by 20 yards and
8 change the legal standards which is what they're trying to do,
9 they must prove an actual adverse effect upon competition in
10 the entire market. That's what the Second Circuit has said
11 repeatedly is the standard here.

12 Now, what their expert said was if we eliminate the
13 NDPs -- let's put aside the fact that this is a two-sided
14 market for a moment. The government suggested today that our
15 whole case depends upon you seeing this as a two-sided market.
16 Well, with respect, Your Honor, we believe you must because
17 that's what it is and indeed your summary opinion already said
18 that the parties seem to agree it's a two-sided market but
19 I'll come back to that as well.

20 Let's assume for the moment you only look at one
21 side, just the merchant side which the government spent
22 virtually all of its time at trial on and all of its time in
23 its closing. What Dr. Katz said was if you eliminate the
24 nondiscrimination provisions, then the merchant discount rates
25 may go up, not down. And if you eliminate those provisions,

1 then product differentiation which is quality of the product
2 may go down and not up.

3 We can find no case -- we've read every Section 1
4 case that the Second Circuit has decided in the last 35 years.
5 We can't find a single case in which a record that says that
6 the price effect which the plaintiff contends is evidence of
7 the anti-competitive effect could actually get worse, not
8 better, and have still found any violation of Section 1. In
9 fact, we can't find a single rule of reason Section 1 case
10 decided by the Second Circuit in 35 years in which a violation
11 was found. In every single one of the cases, the court found
12 that it was not a vertical restraint because when they looked
13 at the market under the proper standard, not the quick look
14 standard that the government would have you apply for the
15 first time in a vertical rule of reason case, the Second
16 Circuit has consistently found no violation.

17 Now, the government has a lot of theories for why,
18 for why the price will go in the direction that they've told
19 you repeatedly it will go if the NDPs were eliminated but they
20 don't have any facts and, in fact, as we'll come to, the facts
21 in the record as opposed to the speculation in the record all
22 go the other way. Every time you look at the factual evidence
23 of what would happen in the absence of the NDPs, the evidence
24 goes against the government's theory which proves, I submit,
25 that there's something wrong with the theory.

1 So what do they do? They change the legal standard.
2 Now, Mr. Conrath said this morning that we're asking the Court
3 to create a brand new standard that's never been used before.
4 With all respect to Mr. Conrath, that simply is untrue.

5 The case law that exists under the Sherman Act and
6 with respect to vertical restraints is a case law that we
7 embrace that doesn't require any tinkering or tampering. If
8 you simply apply the law as it's been written, Your Honor, the
9 outcome here, we believe, is clearly one that comes out in our
10 favor.

11 The government, however, is really putting forth an
12 incredibly shrinking case and what do I mean by that? First,
13 they told you in your papers, I didn't hear Mr. Conrath say it
14 this morning, but they told you in the papers they don't have
15 to prove relevant market, no relevant market is necessary.
16 Then they say, oh, but we proved one, and I'll come to what
17 they actually proved. They said we don't have to prove power,
18 we can do it by direct facts. Well, as Your Honor held, the
19 Second Circuit cases say you can do one way or the other.
20 They haven't done other one here and I'll come to that. They
21 don't have to prove anything on the consumer side of the
22 market. That's a separate side of the market they don't have
23 to contend with. It is not. Every single witness expert who
24 testified here including theirs said it's a two-sided market.
25 Dr. Katz's report in this case is literally full of the

1 agreements with our experts on the fact that it's a two-sided
2 market. Your Honor's summary judgment opinion said the
3 parties already agreed it's a two-sided market. However, they
4 don't think they have to prove anything with respect to half
5 of that market.

6 They don't even have to prove -- and this is where
7 they tried to move the goal post in now even more than they
8 did before -- they don't even have to prove there's an actual
9 adverse effect on competition. All they have to do is show
10 the NDPs, here's a quote, "disrupt the price setting
11 mechanism." They explicitly say, Your Honor, in their
12 proposed conclusions we don't have to prove any actual effect
13 on price. Why do they say that? Because they haven't proved
14 an actual effect on price. Not only have they not proved it,
15 but their expert said it may go the wrong way and the factual
16 evidence is that it, in fact, goes the wrong way, namely, up.

17 So, instead of confronting the evidence, which you
18 didn't hear a word about, maybe Mr. Conrath is saving it for
19 rebuttal. He never mentioned Dr. Katz's admissions. He never
20 mentioned the 3 million plus merchants in the United States,
21 merchant locations, that do not accept American Express and
22 had been subject to Visa/MasterCard degree for the last three
23 plus years. He didn't say a word about them and I'm going to
24 say more than a few words about them.

25 They've changed the standard or they tried. They

1 said all we have to do is to show that the mechanism has been
2 disrupted. I would submit, Your Honor, there's a reason why
3 they call vertical restraints restraints and that's because
4 every one of them restrains some form of competition. The
5 question is whether it's an unreasonable restraint.

6 Merely saying that they don't have to prove any
7 effect on price, just that there's a mechanism that could be
8 disrupted, is not the standard. If it were, take, for
9 example, the resale price maintenance case where the
10 manufacturer tells the retailer it cannot sell its product for
11 less than \$10. That obviously disrupts the pricing mechanism
12 but every resale price maintenance case decided in the Second
13 Circuit in the last 35 years has come out in favor of the
14 defense because they're not unlawful under a full reasonable
15 analysis according to the facts in every one of those cases,
16 yet they would be condemned under the government standard as
17 would exclusive dealing arrangements.

18 Obviously, they disrupt the pricing mechanism if you
19 say, I'm going to sell you all of my product and I refuse to
20 sell it to anybody else. Well, you're going to be able to
21 charge perhaps more for my product than you would if there was
22 intra brand competition and my product was sold to your
23 competitors as well and yet, all of those cases have been
24 found in favor of the defense because they don't violate the
25 rule of reason. What they might well violate, and that's why

1 the government embraces this new standard is the quick look
2 standard.

3 Now, there are three standards in the antitrust law
4 for evaluating conduct: Per se, rule of reason and in between
5 is quick look. All of the quick look cases that they cite,
6 all of them, are horizontal cases which makes sense because
7 the law of per se violations arose originally in the
8 horizontal context of price fixing and that's where it still
9 resides, in a horizontal price fixing case. What's happened
10 is the Supreme Court said, among other places, in the Indiana
11 dentist case they rely on so heavily, there are going to be
12 cases where you look at it, you are going to be able to tell
13 it's so likely that there's a violation that we're not going
14 to engage in what Your Honor described as the most searching
15 form of antitrust analysis, namely, the rule of reason
16 analysis. We're going to take a quick look. And it is in the
17 context of those quick look cases that the language that the
18 government embraces here about only looking at the mechanism
19 and not having to find actual anti-competitive effects is
20 found.

21 I would respectfully submit, Your Honor, that were
22 this Court to apply the quick look standard to this vertical
23 rule of reason case, that would be legal error. It's never
24 been done. We can find no instance in which any rule of
25 reason vertical case has applied the quick look standard, yet

1 it's what the government argues for here and hangs so much of
2 its hat on.

3 The Indiana case is really the quintessential,
4 quintessential quick look case, and if Your Honor looks at
5 slide three in our deck is a quote from the California Dental
6 Association against Federal Trade Commission case in which the
7 Supreme Court says, describes when you apply the quick look
8 standard --

9 THE COURT: It's coming.

10 MR. CHESLER: Thank you.

11 It says, An observer with even a rudimentary
12 understanding of economics could conclude that the
13 arrangements in question would have an anti-competitive effect
14 on customers and markets.

15 That's the -- it's the per se light approach that
16 the Supreme Court adopted. It doesn't apply in this case and
17 yet, the government sites horizontal cases for that standard.

18 The actual standard, Your Honor, is repeated in a
19 number of Second Circuit cases and slide four is two examples
20 of that. One is the KMB Warehouse case from 1995. It's a
21 Second Circuit case.

22 The quote we have put up here, there's several in
23 the opinion and we pulled out one of them which says, Isolated
24 statements of preference -- I like this person's product
25 rather than that -- are not a sufficient "empirical

1 demonstration concerning the adverse effect of the defendants'
2 arrangement on price or quality, quoting, in turn, from the
3 Jefferson Parish case in the Supreme Court.

4 In the Todd v. Exxon case, then Judge Sotomayor also
5 talked about what is required in the actual standard that
6 applies here when she pointed out that the plaintiff will have
7 to make a substantial presentation of evidence to support her
8 claim that salaries would have been higher without the
9 information exchange.

10 Not an expert who comes in and says let the chips
11 fall where they may, maybe the price will go up, maybe the
12 price will go down. Not a plaintiff who's confronted with
13 actual U.S. market conditions in which the price went up, not
14 down. But a plaintiff who makes, in Judge Sotomayor's words,
15 a substantial presentation of evidence to support the claim
16 that salaries or, in this case, prices would have been higher
17 without.

18 Now, to avoid confusion down the road, Your Honor,
19 there are two sections in the Indiana Federation opinion, two
20 separate pieces and one piece has a statement of the law which
21 is pretty straightforward with which, I think, everybody
22 agrees and that is, and certainly the government has argued
23 that in this case, that you can obviate the need to prove
24 market power by proving actual detrimental effects.

25 That's not the portion of the opinion that they

1 quote from. The portion of the opinion they quote from is
2 where the Court recites the quick look standard and talks
3 about disrupting the pricing mechanism and that, as I said, is
4 not the law.

5 They also mischaracterize, Your Honor, other cases.
6 And one that I just want to pause on for a moment because it's
7 a case I'm going to come back to several times is the U.S. v.
8 Visa case, the rules decision, exclusionary rules decision.

9 They say in their conclusion of law, number 20 --
10 let's put up slide five. They say, "Stunting price
11 competition is itself an adverse competitive effect," and they
12 cite U.S. v. Visa. You'll note, Your Honor, that there's a
13 bracket around the "S" in "stunting" and they've capitalized
14 it so we pulled up the actual statement from the Visa case
15 from which they cropped the quote.

16 You'll see it says, The District Court found that
17 Visa USA and MasterCard's exclusionary rules -- let me pause
18 there -- harm competition by reducing overall card output --
19 that's an affirmative finding of an actual adverse effect,
20 reducing output -- and available card features which is
21 innovation, reducing innovation, as well as by decreasing --
22 not the possibility, but an actual adverse effect --
23 decreasing network services output -- and then comes the
24 phrase -- and stunting price competition.

25 They've excluded the whole front end of the sentence

1 in which all of the actual adverse impact language appears
2 which is the standard that the Court applied in U.S. v. Visa
3 and they cropped the quote for the last three words suggesting
4 to Your Honor in this finding, in this conclusion, I should
5 say, and others, that they need not prove any actual affect on
6 price. Just affecting the mechanism is enough.

7 I would submit, Your Honor, they simply can't move
8 the goal post that way. The legal question, as I said, is
9 whether there's an actual adverse effect upon competition in
10 the relevant market and part of the problem here, part of the
11 problem is that we in the government, although the government
12 gives lip service to this being a two-sided market, we
13 fundamentally disagree on what that means. The government
14 says we're asking you to do something that's never been done
15 before and, again, we respectfully disagree.

16 We're asking Your Honor with great respect to apply
17 the law as it exists. The law says you must find an actual
18 adverse effect upon competition in the relevant market.
19 That's where the dispute exists. The government says the
20 relevant market is for merchant network services and
21 Mr. Conrath stood here today and he said to you, oh, American
22 Express's definition of the network, and he pointed to one of
23 Professor Gilbert's exhibits showing that the network goes all
24 the way around from merchants to consumers, that can't be
25 right.

1 And what was Mr. Conrath's explanation for why it
2 can't be right? He said, well, you can't substitute one part
3 of the market for another, they're not reasonably
4 interchangeable. That's a remarkable statement from somebody
5 with as much antitrust experience as Mr. Conrath who is as
6 learned in the field as I know he is. Let me give you an
7 example. Suppose the relevant market is for men's suits.
8 Would anybody suggest that you could wear two pairs of pants
9 instead of one of the jackets? Do all the components of the
10 market have to be interchangeable with one another for there
11 to be a market?

12 The question here is whether a transaction completed
13 on AMEX's network is reasonably interchangeable with a
14 transaction completed on the Visa or the MasterCard or other
15 network. It's the transaction. It's not pieces, components.
16 It's not jackets versus pants. It's suits versus suits. So
17 the government, as it does over and over again in this case,
18 asks the wrong question and not surprisingly, it gets the
19 wrong answer. Nor is the question whether you can ignore what
20 happens on one side of the market which is what they accuse us
21 of and look at only one. They say, oh, you can do anything,
22 you can abuse the merchants any way you want as long as
23 there's a benefit to the consumer and American Express says
24 it's okay. Mr. Conrath said, perhaps not in such a colorful
25 phrase as I used, but he made the same point this morning.

1 That, again, is a mischaracterization of our case.
2 We're not suggesting that at all. To the contrary, what we're
3 saying is that the market as it exists today is conferring
4 competitive benefits on both the merchants and on the
5 consumers. I don't think there's anyone in this courtroom who
6 could stand up here and credibly say to you that if we were
7 still a check and cash society, that there would be the volume
8 of gross domestic product in the United States today that
9 there is. No one can say that and be credible. And the
10 reason it's not credible is because so much of the gross
11 domestic product today in America rests on the back of other
12 forms of transactions than cash and check, namely, credit,
13 whether it's bank borrowing or the plastic we carry in our
14 pockets, debit cards, credit cards, et cetera. It increases
15 demand. Where is that demand exercised? Where is the money
16 spent for that demand? It's at the merchants.

17 The idea that we suggest that the merchants are long
18 suffering prisoners of our theory that only the consumers
19 benefit is frivolous. They both benefit. The consumer gets
20 her rewards, the merchant gets his purchase. And the way the
21 consumer gets her rewards is by buying the product at the
22 merchant. Everybody benefits. And if we stop recruiting
23 Cardmembers, then merchants will have no interest in taking
24 our business, and if merchants stop carrying our cards,
25 consumers will have no interest in carrying our cards. That's

1 the network effect in which all three economists agree.

2 You can't, Your Honor, with respect, accept the
3 reality of that network effect and then draw an impermeable
4 membrane down the middle of the market and say, I'm only going
5 to look at half. I'm going to ignore the other side. I'm
6 going to make believe that if a merchant pays more, she is
7 injured, as opposed to a merchant paying more and getting more
8 customers in her store buying more products.

9 Every merchant the government called who we asked
10 are you making more profit with the American Express card than
11 without said yes. It's more profitable for me to carry the
12 American Express card than not. And the way America works, at
13 least as I understand it, if it weren't, they would stop
14 carrying us the way three million plus others have chosen not
15 to and the government has proved nothing to contradict that.
16 Nothing. They just ignore half the market and say that's okay
17 but we're not ignoring it. We're looking at the benefits that
18 this model has provided to both, not to just one side.

19 And, Your Honor, it is not just an American Express
20 argument. Their own expert -- and, again, they never
21 mentioned this today. What did Dr. Katz say? Let's look at
22 slide six. What did Dr. Katz say when I asked him about his
23 testimony on First Data where he was on the other side of
24 Mr. Conrath and his team and he was critical of their theory?

25 It goes on to say, and I was referring to his

1 testimony in First Data, which was a debit network merger case
2 where the government was opposing a merger, "It is critical
3 not to draw unwarranted and misleading conclusions by focusing
4 solely on one side of a two-sided market. I take it you agree
5 that you made that statement in that case, sir? And he said,
6 I agree I made it and I agree with the statement.

7 Your Honor, that's exactly what the government is
8 doing here. They're looking at one side and they're drawing
9 erroneous conclusions, but I say, again, even if you look at
10 only the one side, I challenge them to show you a case in
11 which the government's only economist has ever testified that,
12 in fact, the price effect that they say will come about may
13 not come about and the government prevailed showing that that
14 price effect was anti-competitive. They can't.

15 Indeed, the closest we can find is a case in which
16 the court actually suggested that because there was going to
17 be more affirmative argument, more affirmative statement than
18 Dr. Katz said because there was going to be no change in the
19 price, that the plaintiff lost. They couldn't prove an
20 anti-competitive effect because they couldn't prove that the
21 price would, in fact, go down. Well, that principle, Your
22 Honor -- that's a Second Circuit case. I believe it's KMB
23 Warehouse and if I have the citation wrong, I'll fix it later.

24 Your Honor, they can't prove that the price will, in
25 fact, go down and they didn't prove it. The experts said

1 let's the chips fall where they may, the price may go up. And
2 that brings me, Your Honor, to what we call the natural
3 experiment.

4 The natural experiment is what's been going on with
5 respect to the 3 million plus merchant locations that do not
6 accept American Express, that accept Visa, MasterCard and
7 Discover, and have been subject to the "but for" world that
8 the government conjures up for the last three to four years.

9 Now, as we put in the evidence about this, Your
10 Honor, their competitive impact statement to this Court and
11 the press conference they held the day they announced the
12 settlement both said there will be immediate, immediate
13 pro-competitive results.

14 In fact, the Wall Street Journal asked the
15 government at the press conference, You're telling us that
16 we'll all have to wait to see the results of this until the
17 American Express case is resolved? And Assistant Attorney
18 General Varney said, oh, no, oh, no. There are, she said,
19 4 million merchants in the United States that do not accept
20 the American Express card and you will see the benefits of
21 this settlement immediately.

22 So what's happened? What did Mr. Hochschild of
23 Discover testify under oath happened? The rates all went up.
24 Not a nickel of savings was passed on to consumers because
25 there weren't any savings to pass on. All rates of all three

1 went up. Surely the government can't suggest that we were
2 responsible for that. We're not there. So what do they
3 answer? They've got a bunch of other theories. Well, it's
4 too soon to tell. They're small merchants.

5 Four years, Your Honor, is not too soon. When
6 Dr. Katz was asked how long would he expect to wait until he
7 saw steering to debit after the Durban amendment, he said if
8 it isn't happening in a year, it's not going to happen. They
9 didn't even try to explain why that year shouldn't apply here.

10 Why is four years not soon enough here and a year
11 was soon enough for steering to debit? They said, well, it's
12 smaller merchants. The merchants who do not accept American
13 Express are the same size as 98 percent of the merchants who
14 do accept American Express. So, if the government genuinely
15 means that you shouldn't expect to see any change, you
16 shouldn't expect to see any decrease in merchant fees for the
17 98 percent of our merchants, then what they're telling you is
18 they brought this lawsuit for the 2 percent of the merchants
19 because the 98 percent are beyond help according to them. If
20 they stand up on rebuttal and they say, oh, no, we brought it
21 on behalf of all the merchants, then I would like to know how
22 come the prices have gone up at the 4 million or 3 plus
23 million merchant locations that we're not present at.

24 So, I can't predict the future, but I can read and
25 I've read what Mr. Hochschild said, indeed, he said it in

1 response to a question I asked. In fact, I was here. So were
2 you. He said the rates went up at all of those the merchants.
3 So, what's the actual evidence of fact of what happened, not
4 theory of what may happen in the new world, what's happened?
5 The rates have gone up.

6 I would, I would suggest, Your Honor, with great
7 respect, that to draw an inference from the government's
8 suggestion because 12 merchants came in and said, I think if I
9 can get rid of those darn NDPs, my rates would go down, I
10 could play these guys off against each other as if they were
11 selling couches to IKEA in a one-sided market, that's what the
12 guy from IKEA said, to base it on that when their own expert
13 said they might well go the wrong way and three plus million
14 merchants are paying more today than they were before in the
15 "but for" world the government conjures up would be an error.

16 THE COURT: It might be that the Visa and MasterCard
17 are smarter than whoever that person was at the Justice
18 Department who made the comment and they decided, well, as
19 long as we have the cover of American Express with their
20 anti-steering provision, we're not going to go out and tell
21 the merchants that they can go out there and steer because we
22 can just raise the price until the AMEX case gets resolved.

23 MR. CHESLER: Your Honor, that's a theory. There's
24 not a shred of evidence.

25 THE COURT: No, but what I'm saying is they have,

1 Justice Department had its theory and I can't divine why it is
2 that there isn't competition where there's the ability to
3 compete with one major exception, and that is that the AMEX
4 NDPs.

5 So, you know, I mean, I understand your argument,
6 but there are, you know, I'm a judge, you know. I didn't go
7 to the Harvard Business School. I assume this will be a, if
8 it isn't already, a project or a case at Harvard Business
9 School at some point. I don't know what it will say, but it
10 will be out there and I'm thinking, you know, that it's an
11 unresolved issue. So, for you to argue that it didn't happen,
12 it's because it's not a completed process.

13 Isn't that really what's going on here?

14 MR. CHESLER: I don't think so, Your Honor, and let
15 me say why.

16 I'm not suggesting there aren't --

17 THE COURT: And I'm not disparaging the Assistant
18 Attorney General.

19 MR. CHESLER: I'm very happy, on the basis of joint
20 and several liability, Your Honor, I'm thrilled to hear it. I
21 may add had you gone to the Stern School at NYU, there might
22 be a case on that subject.

23 THE COURT: That was my mistake.

24 MR. CHESLER: Your Honor, I'm not suggesting there
25 aren't many theories that one could offer for why. I'm making

1 I think a simpler point and my point is this.

2 If you look simply at the facts, I think we all
3 agree in this record the facts are there are over 3 million
4 merchants for whom our NDPs don't exist, who are not subject
5 to the Visa or MasterCard NDPs because of the decree, and
6 their rates went up. That's a fact. And all I'm saying is
7 when you look at the theory the government supplied, it was
8 delivered by Dr. Katz who didn't say, I can tell you with
9 great confidence and, in fact, without exception the rates in
10 fact will go down. He said they may well go up. In fact, he
11 pointed out, as it's true, after the exclusionary rules case
12 was decided, the rates did go up.

13 Why? Why did the rates go up after the exclusionary
14 rules? Because of the competition that was unleashed on the
15 consumer side of this two-sided market which the government
16 says is not part of the same market, they were now competing
17 for the consumers and they raised the rates for the merchants
18 to provide funding to generate and fuel that competition on
19 the consumer side. So, in fact, after the government won the
20 exclusionary rules case, merchant fees went up. Dr. Katz
21 there predicted they would and he was right. By the way, the
22 government said that would be a good thing.

23 Why was it a good thing in the exclusionary rules
24 case? Because it was going to foster competition among the
25 consumers. Now they say higher rates would be a bad thing and

1 they said they sued us to guarantee lower rates. They didn't
2 tell you that they sued us because the lower rates might
3 happen. They told you they sued us because the lower rates
4 would happen and their economist doesn't agree with that and
5 the facts in the record don't agree with that.

6 By the way, Your Honor, they mentioned Canada at one
7 point in the proceedings, the rules of conduct that have been
8 implemented in Canada. What's happened in Canada? Rates have
9 gone up. That's two. They mentioned Australia where the
10 government, unlike this government, regulated rates and
11 slapped a lid on Visa and MasterCard rates at half or I think
12 a quarter of what they were before. What happened there? The
13 consumer fees went up and the rewards went down. The idea
14 that these are not an inexplicably linked two sides of one
15 market is simply inconsistent with everything in the record.
16 Whether you look at Canada, whether you look at Australia and,
17 most importantly, whether you look at the United States, they
18 have no factual scenario.

19 So, back to your suggestion of why, that may be the
20 answer, Your Honor. I don't know and you don't know. What I
21 do know, though, is if you look at the facts in the record,
22 every one of these goes the wrong way for them and their own
23 messenger didn't deliver the message as he was planning to
24 deliver it. He said no, it could go the wrong way too.

25 Now let's come to Mr. Chenault. You asked

1 Mr. Conrath. You said you were saving that question for me.
2 Let me preempt that by answering that question if I may.

3 Mr. Chenault lived through the history of what
4 happened in what the government says was competition on the
5 merits. It almost destroyed his company. We saw and heard
6 the architect of that strategy. He was on the stand.

7 Mr. Morgan. We saw the contemporaneous report he delivered to
8 their board in Cannes, France. He drew exactly the same
9 circle in his Visa document never having seen Chenault's
10 presentations of the circle of our model. He drew the model
11 and he put a big fat "X" through the merchant fees.

12 This wasn't competition on the merits. This wasn't
13 I'm going to do their playbook one better. This was I'm going
14 to choke off the funding for their point of sale relationship
15 so that they can't fund those pesky rewards and what will we
16 do? We will blast them back into a niche.

17 By the way, a niche which the government tells you
18 is a standalone relative antitrust market, travel and
19 entertainment which I'll come back to.

20 Their strategy was laid out in simple English almost
21 20 years ago. Cut off the funding and it will kill them. And
22 the American Express company lost one-fifth of its entire card
23 business in the United States in four years. Mr. Conrath said
24 there was a lot of stuff going on, they were trying to be a
25 supermarket. Where is the evidence that that had anything to

1 do with the near death of the company? There's no evidence.
2 That's just a guess.

3 What the chairman of the board said -- he put
4 himself in a public courtroom with stock analysts standing in
5 the back. I've never seen a CEO of an American company who
6 had the courage to do that, Your Honor. The guy from Visa
7 that they keep pointing to, he was running a nonprofit
8 association owned by a bunch of faceless banks standing behind
9 him. He wasn't the CEO of a public company who stood and sat
10 in a public courtroom and told the stock analysts that if I
11 lose this case, it might well kill my company. He did that
12 because he lived through the history.

13 Now, to use your point, and the answer to your
14 question is I agree with you. It was a dramatic statement to
15 make a point. That the government would put American Express
16 in harm's way at a world of uncertainty, for what? A theory
17 which their own expert wouldn't sign up for. A theory which
18 is contradicted by the real world evidence that's happened at
19 those 3 million merchants over the last three or four years.
20 That was the point.

21 By the way, it wasn't, as the government suggests,
22 inconsistent with or not supported by anybody else in American
23 Express. That's a remarkable statement. Four other
24 executives came here.

25 THE COURT: No, I know what Mr. Gilligan said.

1 MR. CHESLER: Thank you.

2 THE COURT: I was here for the six plus weeks.

3 MR. CHESLER: That's how I recall it.

4 THE COURT: Yes. Go ahead.

5 MR. CHESLER: So let me go on. I've talked about
6 the experiment. I've talked about the foreign --

7 THE COURT: I don't want you to get too excited
8 because your message is being received. Would you like
9 something stronger?

10 MR. CHESLER: Do you have any sedatives up there,
11 Your Honor?

12 THE COURT: If you keep this up, I might need it.
13 Go ahead.

14 MR. CHESLER: Okay. The government also says that
15 our position is that merchants will not steer. Your Honor, we
16 wouldn't be here if we thought merchants wouldn't steer. We
17 could have done what Visa and MasterCard did, give them
18 sleeves out of our best settlements and go, fine. They agreed
19 to that because no one is going to steer to us from them
20 because they don't have our cards in their wallets. Steering
21 can only go one way here.

22 The record is, I don't think it's in dispute here
23 that most of our cardholders, almost all of them have the
24 other cards. A very small percentage, one-third, different
25 estimates, about one-third of their cardholders have ours.

1 You cannot, as Dr. Katz admitted to me, you cannot steer a
2 consumer to a card she does not have. So, of course, Visa and
3 MasterCard agree.

4 Our position is that steering will happen, not that
5 it won't happen, and when it does, it will create the very
6 uncertainty that Mr. Chenault was talking about.

7 Now, there's another factual basis in the record,
8 Your Honor, to demonstrate that the government's theory is
9 wrong. Beyond Australia, beyond Canada, beyond the 3 million
10 plus U.S. merchant locations, and that's the theory that they
11 have about Discover. They say Discover can't harm
12 competition. We didn't sue Discover because their share is so
13 low, that they can't harm competition. American Express has
14 got five times the charge volume that Discover has so we sued
15 American Express but not Discover.

16 Well, how about the many, many merchants in the
17 United States where according to the evidence in the record,
18 AMEX share has been as low as Discover's share has been? Five
19 percent, 6 percent, 8 percent. Why isn't the government's
20 "but for" world in existence there? We can make a lot of
21 theories for why. I'm just sticking to the facts.

22 It's not just that it's not happening where we don't
23 compete at all. It's not happening where, according to the
24 government's theory, it should be happening because we can't
25 harm competition. We can't be a threat to Visa and MasterCard

1 with 4, 5, 6 percent of the spend just like Discover according
2 to them can't stop it and yet it's not happening. And the
3 reason Your Honor, I submit is clear. Visa and MasterCard
4 don't compete against each other. They are, in fact, a
5 duopoly.

6 They in fact have either three-quarters or
7 80 percent of the market depending on whether you put debit in
8 the market or not. And I would submit, Your Honor, as we're
9 thinking about and as you go back to Chambers and you think
10 about the reasons for why the record is what it is, I would
11 submit that the most plausible, most realistic and most
12 consistent with the evidence reason is that Visa and
13 MasterCard don't compete against each other. If they did,
14 they would be competing now at those merchants. If they did,
15 they would run over us like a road kill at the merchants where
16 we have five percent like the government says they could be
17 doing with Discover. They don't compete. They were born as
18 twins. They still act as twins.

19 You may remember one of the witnesses said, I think
20 it was Mr. Moore, that Visa and MasterCard were like two
21 entrances to a clubhouse at a single country club. That's the
22 way he described them at the time he was giving his speech in
23 Cannes. That's exactly what they are. Oh, yes, they're
24 public and owned by separate groups of shareholders and maybe
25 overlapping. When you look at their boards, there are a lot

1 of bank representatives on the boards. The reality is that if
2 you left the two of them alone, this market would be
3 dramatically different from what it is today and it would not
4 be for the better. It would be for the worse.

5 So, Mr. Chenault didn't tell you, didn't give you a
6 written guarantee that his model will die and his company will
7 die, but what he said was there is a real risk that it will
8 and the question is what's the other side of the weight, what
9 is the other side of the scale Your Honor must balance against
10 that real risk, a risk which almost came to fruition 20 years
11 ago in the We Prefer campaign. The alternative is the
12 government's theory with all the factual scenarios of all
13 those merchants and all those situations going the wrong way.

14 So, what did the government actually prove? They
15 called a dozen or more, 15 merchants, and say I would like to
16 pay less. And if I didn't have NDPs, I believe I would pay
17 less. Well, Your Honor, as I said in the opening, everybody
18 would like to pay less for everything. That doesn't equal an
19 antitrust violation.

20 In fact, the government says, well, AMEX's prices
21 have increased over time. No, they haven't. Even Dr. Katz's
22 price chart which Mr. Conrath put up this morning, while it
23 doesn't have as dramatic a slope down as the Bernheim chart
24 does, it's drifting down, not upward. So, the prices have not
25 gone up.

1 In fact, if we look at slide 15, there's going to be
2 a blank on the screen because this is confidential data, but
3 it's in your book, Your Honor. This is a chart that
4 Professor Bernheim used which covered the time frame of 2002
5 to 2010 in which he talked about what actually has happened to
6 the AMEX rates over that period of time with respect to their
7 merchants.

8 There's no support in the record for the suggestion
9 that the prices, using merchant discount rate as the price and
10 ignoring the two-sided price. There's no evidence the price
11 has gone up. The evidence is the price has gone down and the
12 slope depends upon whether you look at our expert or theirs
13 but both of them go down.

14 (Continued on next page.)
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1 MR. CHESLER: In fact, your Honor, the government
2 suggested the prices are too high. And I would submit there
3 is no evidence in the record to support the proposition that
4 as a matter of antitrust law, our prices are too high.

5 In order for a plaintiff to prove that a price is
6 too high for anti-competitive purposes, for antitrust
7 purposes, they have to demonstrate what the price would be in
8 the absence of the restraint. In fact, if this were a private
9 case, the plaintiffs would have to be able to prove, Here is
10 what it would be without the NDP, and here is what it is, and
11 I'm entitled to my damages.

12 The government doesn't have to prove damages. It
13 has to prove an actual adverse effect. Mr. Conrath didn't
14 refer to, in fact they didn't prove, what the price would in
15 fact be in the absence of the restraints. They just said,
16 It's too high.

17 Well, saying it's too high doesn't constitute an
18 antitrust violation, and saying if there were steering, the
19 prices would go down, we doubt whether that would actually
20 happen given what's happened that the price, to the discount
21 rates. But suggesting it would go down doesn't prove it was
22 too high to begin with. Prices are only too high for
23 antitrust purposes if they are supra-competitive prices.

24 Suggesting that AMEX's price is higher than Visa's,
25 putting aside the fact that the premium is gone, pointing to a

1 particular merchant and saying, American Express got whatever,
2 twenty basis points and Visa got 220, therefore, it's too
3 high, with respect, that doesn't prove it's too high. It
4 proves the arithmetic. It proves the AMEX price is higher
5 than the Visa price for a different product that's in the same
6 market. It's higher. That's all it proves. And there's
7 nothing illegal about that.

8 Cars compete with other cars, where the prices
9 differ dramatically because they are differentiated. Airline
10 tickets compete with airline tickets, and yet one airline
11 charges more to get to a same city from another one because
12 they believe they have differentiated their product and they
13 can charge more.

14 The fact that AMEX has a higher rate at some
15 merchants than others is proof of nothing other than it has a
16 higher rate at some merchants' than others. The unrebutted
17 testimony from four separate witnesses, Chenault, Quagliata,
18 Gilligan and Flindon, the unrebutted testimony is that on the
19 mix-adjusted basis, which their witness Mr. Hochschild
20 admitted is the fair way to compare prices in this industry,
21 there is no American Express premium. It's gone. They say
22 the market is broken. There's no competition. It's gone
23 because there is competition.

24 The AMEX prices have come down. Whether you look at
25 two sides or one side, they have come down, and Visa and

1 MasterCard have gone up. Why have they gone up? Because they
2 have enormous market power, that's why. They control seventy
3 percent or eighty percent, depending upon how you count, of
4 the market.

5 One other reason they have gone up, because the
6 government won their case fifteen years ago. Every time we
7 turn on the TV and every time you stop at an airport and look
8 at the sign on the wall telling you what's in your wallet,
9 that competition is being driven by what the government did
10 and what my client has done and what Visa and MasterCard have
11 had to do. Your Honor may remember that there's a document in
12 the record in which Chase says, We're copying the AMEX
13 playbook. They are not doing it because they want to. They
14 are not doing it because they feel like it. They are doing it
15 because they have to.

16 Why do they have to? Because we are differentiating
17 a product and offering rewards to people that they were not
18 offering. They have not only matched this, I think
19 Mr. Chenault said, They are ahead of us now. We have to catch
20 up. We have to invest more on the consumer side to catch up
21 to them, because they have lapped us in some respects. They
22 are not doing that because they feel like it. That's in fact
23 the competitive market, which the government says is broken.

24 (Pause)

25 THE COURT: Let's proceed.

1 MR. CHESLER: Thank you, your Honor.

2 Several more points on this competitive-effect
3 issue.

4 First, the government says these are two separate
5 markets, one involving merchants, one involving consumers.
6 They cite you to cases, the Philadelphia National Bank case,
7 the Topco case, which they say stands for the proposition that
8 you cannot defend diminished competition in one market on the
9 basis that there's an increase in competition in another
10 market. That is an unremarkable proposition, with which we
11 agree. It doesn't have anything to do with this case. This
12 is a case that involves a market.

13 I'll say it one more time and I'll stop. Even if
14 you only look at half of their market, their competitive
15 effects case goes the wrong way. I said before that we are
16 not asking your Honor to apply a new principle of law, but
17 rather the long-existing principle of law that they must prove
18 adverse effects in the market.

19 I would cite, if you look at slide seven, this is a
20 quote from the KMB Warehouse case in the Second Circuit from
21 1995, in which the court states the often-repeated test in the
22 Circuit, "KMB has thus failed to come forward with any
23 evidence that defendant's actions adversely affected service,
24 quality, or price, market-wide."

25 What is in the market is a case-by-case

1 determination based on the facts in that case, but the law
2 that you must look market-wide for the effects is long
3 established, and that case, among many others, says that.

4 I said to your Honor before that there was a case in
5 which the plaintiff's evidence showed that the price would
6 remain the same if the alleged restraint was eliminated, and
7 the Court said that was dispositive and fatal to the
8 plaintiff's case.

9 I said I thought it was KMB Warehouse, and I might
10 have misspoken. I did. It's the Capital Imaging case. This
11 is slide 12. Here, the Second Circuit says, in 1993, but
12 Capital concedes in its brief, that whether or not it is
13 admitted into the physicians' association -- there was a
14 physician wouldn't let the plaintiff in -- the fee for
15 radiological services would remain the same.

16 And it goes on and says, "Therefore, Capital has not
17 made an adequate showing of a detrimental effect to obviate
18 the need." They didn't say that the pricing mechanism has
19 been tampered with. It was. What they failed to do was show
20 that the prices were in fact higher than they would be. And
21 when the Court made the finding that they hadn't shown that,
22 the Court dismissed their claim. And that, your Honor, is the
23 problem with the government's case here. They have not shown
24 they are in fact higher. They are aspirational, said they
25 think they are higher, but they have not proved it.

1 Your Honor, I was going to spend some time, which I
2 don't think I need to, frankly, on the testimony of the
3 various American Express executives on what they foresee as
4 happening to them and their business were this to go away. I
5 think that you have that in mind, and I am not, in the
6 interest of time, going to spend time on that.

7 I do want to spend just a few more moments on the
8 Visa We Prefer matter. I wanted to show your Honor, so we
9 have it in front of you-- and I have it specifically referred
10 to here, slide 28 -- this was the diagram that I mentioned
11 before that Mr. Morgan used, not for trial but many, many
12 years ago he was planning his campaign. As he says in the
13 testimony next to it: "And you thought breaking the success
14 cycle would pressure American Express' merchant discount and
15 weaken their financial --

16 "Yes.

17 "You also thought that if you could break the
18 premium of price success cycle, you could encourage consumer
19 preference for Visa and keep AMEX as a niche product, right?

20

21 "Yes."

22 Mr. Chenault lived through it. He made what he
23 called his call-to-arms speech eighteen years ago, long before
24 he was even called as the government's star witness in the
25 Exclusionary Rules case, let alone had any inkling in his head

1 this case would take place. This was not a
2 made-for-litigation position. He said what he said it was.
3 It was a call to arms.

4 What he said in that speech was without Welcome
5 Acceptance, our investments don't matter. They are for
6 naught. They won't help us. They won't drive the
7 competition, because our customers will be scared away and,
8 therefore, none of it matters. You can make all the
9 investments you want up front. If at the end of the day
10 people aren't in fact using your card, the investments don't
11 matter.

12 Now, the government suggests that Welcome Acceptance
13 is a pretext of some kind to insulate American Express from
14 competition. It is exactly the opposite, your Honor. It is a
15 competitive force that American Express has spent a fortune
16 developing for decades, so that it could survive and prosper
17 in a market dominated by other networks.

18 I think Mr. Silverman perhaps stated it best. He
19 said in a network-effect market -- remember, he's the young
20 fellow who runs the consumer side of the American Express
21 business, came from one of the Internet companies -- he said,
22 In a network-effect business, where you don't get consumers if
23 you don't have merchants, and you don't have merchants if you
24 don't get consumers, you either have to be the biggest or the
25 best.

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American Express is never going to be the biggest, no matter what it does. The deficits are too great. The lingering effects of the exclusionary rules and the agreements that were entered into with the banks after the exclusionary rules, which have essentially preserved and perpetuated many of the adverse effects of those rules, continue as real forces in the marketplace.

There are seven banks I think that issue American Express cards. There are 10,000 that issue Visa and MasterCard, etcetera. We are the smallest cards in location and force. They are never going to make up the deficit. They have to be better.

What Mr. Chenault got on the stand and said was, In some respects today, we are not better, because some of the competitors are doing a very good job of duplicating and even improving upon our playbook, so we have to be vigilant to jump ahead of them again. That is not, I submit, a description of a broken market. It is a description of the paradigm of a competitive market.

The evidence about the Visa campaign also showed that Visa was acutely aware of something your Honor heard a lot about during this case called the spilling-over effect.

If you look at slide 30. Mr. Morgan was asked: "And you were asked about this at your deposition. You

1 understand the point that is reflected here is that the We
2 Prefer Visa campaign may influence consumers beyond just the
3 store that displays the We Prefer signage; right?

4 "Yes, I do.

5 "That's what it means by, no matter what kind of
6 cash register you are standing in front of; right?

7 "Yes.

8 "So, even though you've got We Prefer at T&E
9 merchants, even if you are standing in front of a cash
10 register Everyday Spend merchants or a home retailer, the way
11 you designed this program was that We Prefer could influence
12 behavior in all those circumstances; right?

13 "Right."

14 That's, again, a feature of this market, which is
15 different from many other markets. And there's tons of
16 evidence in this record about how what happens at a merchant
17 affects what happens at other merchants.

18 There was the example of losing the Continental
19 lounge, and AMEX spend levels in the State of New Jersey
20 declined, not just at the lounges and not just at the airport.
21 There's the example of making a deal with Safeway, and
22 spending in the store near Safeway stores went up. That's the
23 spillover effect.

24 What Visa understood as acutely as American Express
25 did is, if they could choke off the point of sale, if they

1 could kill the funding source for the benefits to consumers,
2 it was not just putting the AMEX model in jeopardy, blasting
3 them back to be a niche T&E supplier, the spillover effect of
4 doing that would hurt them across the board. And that is why
5 they lost a fifth of their entire card business in four years,
6 because it has a spiraling, snowballing effect.

7 The empirical studies that are in evidence show that
8 AMEX's network remains today highly sensitive to spillover.
9 And slide 32, which is from an internal AMEX document,
10 DX 404 from 2007, many years after the We Prefer campaign,
11 demonstrates that the spillover effect still takes place. You
12 see it's says, in the highlighted area, "Twenty-five percent
13 of the card members suggest that such experiences do affect
14 future usage propensity." They look at it all the time, your
15 Honor, because it's so important to the success of their
16 business and their ability to compete

17 And you may remember, there was some questioning of
18 Dr. Katz, in which he conceded, and if you look at slide 34,
19 this is from Dr. Katz's examination, we were looking at a
20 study that was done of the impact that writing about in the
21 economic literature about the Everywhere You Want to Be
22 campaign, and the We Prefer, Everywhere You Want to Be came
23 before the We Prefer.

24 The data we are talking about at this page of the
25 transcript shows, in terms of their cardholder tracking study

1 of consumer perceptions of which card is accepted by more
2 merchants, American Express starts at twenty-five percent.
3 After Everywhere You Want To Be, they are down to eight. But
4 after We Prefer, it's cut in half again, and they are down to
5 nine. It was working.

6 Whether you agree with Mr. Chenault's ultimate
7 observation or not, he lived through that history. He saw the
8 power of what would happen to that business model, which
9 fourteen years ago the government allowed was the best hope
10 for this industry, and he saw, he, Mr. Chenault, saw what
11 could happen to it in the face of exactly the relief that the
12 government is asking for here.

13 By the way, I won't stop on it now, slide 35 in your
14 book shows as recently as three or four years ago, Visa was
15 looking at another campaign, in which they said there would be
16 a contagion effect by -- again, that's just the provocative
17 word for spillover -- a contagion effect on American Express's
18 use at other merchants as a result of the strategy they were
19 considering to do at the time. So, it's not competition on
20 the merits, your Honor. It's real, and he lived it.

21 And if you look at Mr. Hochschild's testimony at
22 slide 38, I was asking him here about what happens if a
23 customer has a negative experience at the point of sale:
24 "Isn't it also the case that if the customer has a negative
25 experience at the point of sale as a result of the merchant

1 attempting, for whatever reason, to get her to use a different
2 card, that that can impact the customer's perceptions of the
3 product, their perceptions of your brand, the likelihood that
4 they will continue to use it, so that that can be detrimental
5 to the relationship you have with your customer? Don't you
6 agree with that, sir?

7 "Yes."

8 He admitted elsewhere in his testimony that Discover
9 adopted its own nondiscrimination provisions in order to
10 attempt to protect itself against that kind of
11 life-threatening conduct. Now, he had explanations about, Oh,
12 ours aren't really the same as AMEX's. When I showed him the
13 language, they are the same. I asked him if he told his
14 merchants they were not really the same. He said, No, we are
15 in the process of working that out.

16

17 Again, what he may do in the future is speculation.
18 What we have now is NDP's that look almost exactly the same as
19 ours and implemented for the same reason. The only difference
20 is, the government didn't sue them, because their shares are
21 too low and they are not worried about them. Yet they put all
22 their chips -- and I heard Mr. Conrath say today they are
23 putting their chips on the Discover box in the roulette board.
24 There was protectionism. American Express is here urging
25 protectionism. Discover is the answer. Free them up from the

1 bonds of these NDP's, and they'll set you free. They are like
2 the old Washington senators. They have been in the basement
3 for twenty-five years. They have never left twenty-five
4 percent of the market.

5 You heard what Mr. Hochschild said when I asked him,
6 Why aren't you pursuing this strategy at the merchant where we
7 don't do business, where you don't even have NDP's Visa and
8 MasterCard? He said, Well, we looked at the top hundred.
9 They all had American Express as a vendor, as well, so we just
10 closed down the committee.

11 The only evidence in the record of how much business
12 is available at the three million-plus merchant locations that
13 he walked away from was Mr. Bernheim's estimate of \$280
14 billion of spend every year. Mr. Hochschild thought perhaps
15 it was not important enough to look at that. So, what's
16 happened to his rates? Has he pursued the strategy which the
17 government thinks he's going to pursue, which the government
18 wants you to implement here by deciding against us? Again,
19 theories. You can have lots of theories. What are the facts?
20 The facts are that he's had an opportunity for the last three
21 and a half years to do exactly what he says he would do, and
22 he hasn't done it.

23 Instead, he's raised his rates. When he was asked
24 why, he said, After I looked at the top hundred, I gave up, so
25 I ignored the \$280 billion that was sitting out in the

1 marketplace. Maybe that's why he's at five percent of the
2 market. Maybe those kinds of business judgments have
3 something to do with that.

4 What we do know about the facts is, he didn't do it.
5 Frankly, when you look at the Visa and MasterCard documents,
6 tons of which are in this recorder, you will look long and
7 hard to find any references, let alone any suggestions, that
8 they take Discover as a serious threat. They are filled with
9 AMEX references. They don't care about Discover. Discover is
10 almost meaningless to them, for the reason that the government
11 didn't sue them. They can't hurt anybody. There aren't
12 enough people using the card. There isn't enough spend volume
13 on the card. The idea that -- take any one of the merchants
14 that they put on the stand, take Sears, take any one of them,
15 Ikea --

16 THE COURT: Take Walgreens.

17 MR. CHESLER: Let's take Walgreens. Remember what
18 Mr. Rein said. I'm going to spend a few minutes on him before
19 I finish today. Mr. Rein said the reason he reversed his
20 decision after a sleepless night, having announced he was
21 cancelling us publicly after he got whatever complaints he
22 got, he then cancelled those. When I asked him why, he said,
23 Because I didn't want to disappoint or inconvenience my
24 customers. I didn't want to inconvenience them.

25 He was advertised as an insistence story by the

1 government. He was going to prove that, We have market power,
2 antitrust market power, by virtue of insistence. He didn't
3 prove anything of the sort. He had a thousand complaints with
4 over 800,000 American Express customers. He had an in-house
5 expert who said, We could lose 5.3 percent of the AMEX spend
6 and be fine.

7 1,000 complaints out of 850,000 customers is so much
8 less than 5.3 percent. It's a tiny decimal point lost in the
9 rounding. Why did he say he reversed himself? Because he
10 didn't want to inconvenience any customers. That's what he
11 said. Okay.

12 Well, he carries Discover for the same reason.
13 Think about the likelihood. Think about the likelihood that
14 he's going to tick off -- to hopefully use a politically
15 correct phrase in this courtroom -- his Visa and MasterCard
16 customers by steering them to Discover.

17 Visa and MasterCard have -- I don't want to misstate
18 the record -- it's something like three-quarters or more of
19 the American Express's share of the spend at Walgreen's as
20 single digits, and Discover was about the same size. Let's
21 assume they were both seven percent. The two of us together
22 were fifteen percent. That means Visa and MasterCard are 85
23 percent of Walgreen's spend.

24 Is it realistic for your Honor to presume, given
25 that Walgreens got on the stand and sorry that he reinstated

1 us because he didn't want to inconvenience any customers, that
2 he would say to the customers who account for eighty-five
3 percent of his purchase volume that, I want you to use
4 Discover? There's no evidence in the record to support that.
5 There's no evidence that he would. He didn't do it in the
6 example the government cited. He didn't want his customers to
7 walk across the street, any customer, to CVS and fill her
8 prescriptions there with our card. That's why he did it.
9 That was his testimony.

10 So, the question is, have they demonstrated, has the
11 government proven, anti-competitive effects? I would say they
12 have.

13 Last point on competitive effects. Free-riding.

14 The cases are legion that say that free-riding is in
15 fact anti-competitive, and rules that prevent it are in fact a
16 good thing. And the evidence shows that in fact, the effects
17 of the marketing campaigns that American Express does with
18 merchants linger well, well beyond the time when the campaign
19 is over.

20 Dunkin' Donuts is a good example, where they said
21 their sales increased from the campaign, continued after the
22 campaign was over. If those customers are steered away from
23 American Express, that's free riding, because that benefit to
24 American Express is taken away. The investment we made in
25 that campaign, the effect of which survive the campaign, is

1 taken away by the steering. That's classic free-riding. And
2 the record also pointed to fixed expenses that in fact will be
3 lost in the event of steering, which is also free-riding.

4 So, your Honor, with that, I want to turn, if I may,
5 to market definition.

6 Now, with respect to the market, as Mr. Conrath said
7 and we agree about that, there are two issues. One is debit,
8 and one is T&E. Let me talk about debit.

9 First, I said, when I said something about the
10 government's incredibly shrinking cases, they say in their
11 papers, We don't have to prove market definition. We prove
12 anti-competitive effect we're done. We have to prove it could
13 be, which I have covered. In fact, they do have to prove a
14 relevant market.

15 And slide 50, two Second Circuit cases, KMB
16 Warehouse and the City of New York v. Group Health, many
17 others cases we could cite, they all say the same thing. Your
18 Honor said it in one of the sentences of your summary judgment
19 opinion. The first step is to prove the relevant market
20 before you go on to the other issues in the case. So, I think
21 the law is pretty clear, in the law of the case as well as
22 this circuit, that they have to prove a relevant market.

23 What does the government do with respect to market
24 definition? Well, they obviously want to keep debit out.
25 There's no secret about that. If you put debit in the market,

1 American Express's share of charge volume is 13.9 percent a
2 year or so ago. I asked Professor Katz, Can you give me a
3 single case where a defendant has ever been found to have
4 antitrust market power with that share? He cited the Vons
5 Grocery case. It's not a vertical case. It's the only one he
6 can think of. We can't find one. Not one. It's obvious that
7 debit has to stay out of the market. Because if it doesn't.
8 The government has a real problem on market power.

9 So, they do two things that I would characterize,
10 your Honor, as an absolutist view of market definition,
11 neither of which we believe is supported by the law.

12 And they are, one, that the competition must be
13 perfect. They must be perfect substitutes for one another in
14 order to keep them in the market. Number two, that the test
15 is an all-or-nothing test. Would you throw away this pen and
16 use only another pen? And if you wouldn't throw this one
17 away, then you haven't proved that the two are in the same
18 market. Neither of those absolutist tests is the law.

19 Let me start with perfect competition. They ask --
20 slides 51, 52 and 53. I won't put them up. They are excerpts
21 from Dr. Bernheim's examinations where Mr. Conrath asked him a
22 series of hypotheticals: Suppose you woke up on Tuesday and
23 you wanted to do one or the other. You wouldn't agree with
24 that, that one is the substitute for the other? It doesn't
25 have to be perfect competition, and that's not in the law.

1 In fact, if we look at slide 54 for a second, when
2 Professor Katz was on the stand, I asked him whether, a
3 question on the same hypothetical, and he said, Well, I said,
4 But you in fact put nonrevolving charge cards and revolving
5 credit cards in the same relevant market, don't you? And I
6 want to pause on the question for a moment, your Honor,
7 because if perfect competition were the standard, if it had to
8 be a for-everyone-in-the-market debit, is always a perfect
9 substitute for credit or charged in order for them to be in
10 the same market, then the government could not have suggested
11 the general-purpose, general-card card market. Revolving
12 credit and nonrevolving credit are not substitutes for each
13 other.

14 There are millions of people in this country who
15 have to carry a balance on their cards, because they can't pay
16 it off in full, and they are prepared to pay the interest as
17 high as they are in order -- because they can't afford to pay
18 the balance down to zero. The government put the revolvers
19 and nonrevolvers in the same market, because they are not
20 perfect substitutes.

21 THE COURT: I think we went through this. I
22 understand your point. This is not associated with the charge
23 card or a credit card that is used as a charge card, like,
24 let's say, one of the noncharge American Express cards?

25 MR. CHESLER: Yes.

1 THE COURT: Yes.

2 THE COURT: Like the Starwood card or the Delta card
3 or one of those other cards?

4 MR. CHESLER: Yes, your Honor, it is.

5 THE COURT: Whereas the debit card has the
6 particular aspect of it where you use it, the money comes
7 right out of your checking account, and it's gone. Basically,
8 a substitute for cash, in the sense that at the point of sale,
9 that money has departed your control?

10 MR. CHESLER: That's right.

11 Just as if you are using a pure charge card, two
12 weeks later, three weeks later, when that bill comes, all of
13 that money also departs your account, because you have to pay
14 the bill in full if you are not a revolving card?

15 THE COURT: Correct.

16 MR. CHESLER: My only point is this. Not that there
17 are not other ways for the company to earn money on the float
18 rather than on fees. Just that they are not perfect
19 substitutes. They are overlapping substitutes. They are
20 reasonably interchangeable substitutes, and the government
21 puts them both in their market. Yet when it comes to debit,
22 as the questions Dr. Bernheim illustrates, the government's
23 argument, is debit and credit have to be perfect or else they
24 are not in the market.

25 When I asked that question of Professor Katz,

1 basically the same hypothetical, he said, Yes, because as I
2 have just testified, I think this focuses on reasonable
3 interchangeability from the customer's perspective, and
4 looking at an individual customer and whether he or she would
5 be willing to switch is the wrong way to look at it. I have
6 to take a quicker perspective in terms of what's happening
7 with customers overall. And then you've got to see what it
8 means in terms of the merchant decision calculus. Then
9 there's no conflict with what I have done there and what I
10 have done. You don't confuse it with the perfect competition
11 model, is what I am saying.

12 Also, with respect to all-or-nothing substitution,
13 that's not the law. And again, let me start with AMEX v. the
14 credit cards that are in the government's market. The
15 government relies itself on testimony of witnesses, merchants
16 who say, I would not cancel American Express, even if it were
17 higher by some significant price than Visa. The government
18 points to that as supposed evidence of our power. But I ask
19 your Honor just to think about that in terms of what they have
20 told you the standard for defining a market is, and
21 Mr. Conrath used it against today.

22 The evidence was, you wouldn't throw one product out
23 and replace it in with the other. They are not in the same
24 market. You have all these merchants saying, I wouldn't throw
25 out American Express. I continue to use it and credit, even

1 if there's a significant price disparity between the two.

2 Well, if that's the case, then the government's
3 evidence with respect to AMEX and Visa, for example, is
4 inconsistent with their theory that it's all or nothing, that
5 unless people will throw out credit cards and use debit only,
6 debit is not in the market. They are not going to throw out
7 AMEX and use Visa only, yet they have them both in the same
8 market.

9 The answer, your Honor, lies in two places. It lies
10 with respect to the consumer side of the market, and it lies
11 with respect to the merchant side of the market. And I would
12 add a third one. It lies in what the networks are saying to
13 themselves about the competition they face. Let me pause on
14 that last one just for a moment.

15 Mr. Gilligan testified, you remember, and he
16 testified to the first presentation he ever made in front of
17 the American Express board, and it was a presentation on what
18 the company's strategy should be coming out of the recession.
19 And they observed that there was a significant move toward
20 debit during the recession, as people tried to be more
21 conservative about their financial affairs and discipline
22 themselves to use cards that would require them to pay it off
23 as they made the purchase, so they wouldn't get out ahead of
24 them on their finances.

25 What was the presentation that Mr. Gilligan made?

1 Well, if we look at slide 55, this is where he was talking
2 about it. He says, Well, these are my speaking points on this
3 slide. The slide was showing that -- I think the trend I just
4 said, that we believed consumer credit card volume was going
5 to shrink coming out of the recession. Debit was growing
6 fast, and we wanted to position charge to be a smarter
7 alternative to debit in the minds of our customers.

8 If we did that, we thought charge card growth would
9 start accelerating, that it would become a growth part of the
10 company.

11 Your Honor, that's a real-world illustration of what
12 we are saying, and there's evidence from all four of the
13 networks internally saying to themselves, Debit is taking our
14 share away of credit. Debit is a significant competitor.
15 It's taking a share away.

16 Here is the president telling the board, We have to
17 sell charge as a good alternative to debit, because otherwise
18 debit is going to take a share away from us coming out of the
19 recession. That's competition. That's the kind of real-world
20 competition that courts look to to players in the market. I
21 know who our competitors are, and I see in the marketplace,
22 and that's what Mr. Gilligan was telling the board.

23 If you look at the consumer side, Mr. Conrath
24 pointed to the government's description here that merchant
25 demand for payment card acceptance is derived from consumer

1 demand. He said American Express thinks that's the endpoint,
2 not the starting point. Respectfully, that's not what we
3 think. We think it's important. We think consumer demand is
4 critical. We have put in evidence on both sides, both
5 consumer and merchant side, and I'm going to take a few
6 moments on that, if I may.

7 So, what does the consumer side first say? We put
8 in evidence about the Federal Reserve Bank, of the Boston
9 survey, where the very provisions that the government says are
10 a critical distinction between debit and credit, security,
11 acceptance, convenience, on all of those parameters, the
12 survey says that the consumers view them as comparable as
13 between debit and credit, yet the government says there's a
14 distinction.

15 Among other things, slide 57, which I'll point out,
16 is a chart that was used in the testimony that went to that
17 point. We also, your Honor, spent a fair amount of time
18 during Dr. Bernheim's testimony on the merchant loyalty card
19 data.

20 To net it all out, without going through each one of
21 the slides, we showed that the majority of the consumers at
22 every one of the merchants from which we had the data, the
23 majority, were using both credit charge and debit. What we
24 also showed is that the same consumers were shopping in the
25 same stores for purchases of the same size, sandwiching back

1 and forth. One day they would use a general purpose or charge
2 card. Another day, they would use a debit card.

3 We also showed when an AMEX card member switched to
4 something else on the next purchase, she was at least as
5 likely to use a debit card the next time as she was to use
6 another credit card, such as Visa or MasterCard. That
7 evidence has never been available in any proceeding about this
8 marketplace before.

9 It wasn't available during the U.S. v. Visa case,
10 and I suspect it would have been quite different fifteen years
11 ago, but it's available to your Honor now. It's again
12 real-world evidence of what real people are doing at stores
13 with the cards in their wallets. If you come in on Monday and
14 you spend \$10 and use your AMEX card and come back on Thursday
15 and spend \$12, and use your debit card in the same store,
16 that's what the loyalty card data showed.

17 When three-quarters or two-thirds of all the
18 customers in the database are using both forms of cards at
19 that store, that suggests that they are competitive
20 alternatives.

21 Now, the government says, Well, what about T&E?
22 They are different. First of all, T&E is thirty percent of
23 our business, which means that 70 percent of our business is
24 everyday spend, and these are everyday spend merchants from
25 which you have that loyalty data.

1 What the record also shows is that the T&E merchants
2 -- I'll come to the merchant side -- they are doing a number
3 of things that again are real-world evidence that debit and
4 credit compete with each other.

5 One thing is, the merchant evidence showed that the
6 fastest growing part of their spend profile is debit, over and
7 over again. It was either their house card or the debit card
8 that was growing the fastest. At that merchant, to buy their
9 product, debit was growing, if not the fastest, then second
10 only to their house card.

11 Second thing it showed was, for many of the
12 merchants, they were not even able to separate out the charges
13 that they were receiving from their acquirers for their Visa
14 credit and their Visa debit charges. They were just lumped
15 together as one charge. They were not even teased out for the
16 benefit of the merchants. They had no idea how it allocated
17 out for them.

18 The third thing the record shows about merchants,
19 that they track blended rates. They are looking at their Visa
20 credit and their Visa debit charges, and they are blending
21 them together for their internal tracking purposes, and they
22 are blending them together when they negotiate with American
23 Express for American Express's merchant discount rates.

24 And the next three charts, the next three slides,
25 are confidential, so I won't put them up on the screen. For

1 your reference, they are 60, 61 and 62. And these are
2 references to specific situations involving the use by
3 merchants of blended rates in negotiating AMEX rates. So, the
4 idea that there's no evidence or insufficient evidence on the
5 merchant side to show that debit and credit in the real world
6 are considered alternatives is simply not so. Let me spend a
7 moment on the Cobrand here.

8 Cobrand, the record shows, is forty percent of
9 American Express's charge volume. It's huge. It's literally
10 forty percent of their business. And we had, your Honor, over
11 and over again, examples of Cobrand negotiations where the
12 merchant was insisting upon the right to issue a Cobrand debit
13 card, and since AMEX doesn't have a debit card, they were
14 insisting on the right to issue somebody else's brand debit
15 card, and the evidence from several different witnesses was
16 that American Express resisted that. Why? Well, the
17 evidence, the testimony was, We resisted it because we were
18 afraid of the impact that a Cobrand debit card would have on
19 our charge volumes and our charge fees.

20 (Continued on next page.)
21
22
23
24
25

1 (CONTINUING)

2 MR. CHESLER: Again, Your Honor, that's not a kind
3 of artificially constructed laboratory experiment for the
4 courtroom. It's real world negotiations between merchants and
5 American Express. And the merchants were insisting in some of
6 the negotiations, the evidence showed, that in order for
7 American Express not to agree to a co-brand debit card, they
8 would have to make concessions on the co-brand charge card
9 relationship as an incentive for the merchant to back away
10 from the demand for a co-brand debit card.

11 Again, that's merchant side evidence. Blended
12 rates, co-brand negotiations. All of these pieces of
13 evidence, the soaring percentage of spend on debit are all
14 merchant side evidence, which is quite consistent with the
15 consumer side evidence of what's happened in the last six,
16 eight years in the marketplace with respect to debit.

17 And lastly, Your Honor, the networks. Again these
18 are confidential, so I won't put them up on the screen, but if
19 Your Honor looks at slide 63, 64, 65, you will see competitor
20 networks. Internal contemporaneous documents in which they
21 are telling themselves -- not for publication, but for their
22 own business purposes -- that debit is taking share away from
23 their credit products, that they have to respond, they have to
24 take action with respect to the competitive threat posed by
25 debit.

1 And slide 66 is a very similar statement, this one
2 from American Express. Consumer payment method is migrating
3 from credit to debit. That's what all the networks are saying
4 to themselves.

5 What does the Government say? Well, the Government
6 says use a SSNIP test. Professor Katz says well a SSNIP test
7 is a way -- not the only way he can see, it's only a way --
8 and he concedes that he's not used it in every case. As
9 Mr. Conrath said Professor Bernheim cited a case in which he
10 didn't use it. And what Professor Bernheim explained is that
11 a SSNIP test is only a valuable additional tool when you have
12 quantitative price-related data, which nobody had here. And
13 if you don't have quantitative price-related data that you can
14 put into your SSNIP model, all you're doing is expressing the
15 qualitative competition you've seen elsewhere through the lens
16 of a different test, the SSNIP test.

17 And, in fact, Professor Katz did a regression which
18 I asked him about in one of his reports, after the Durbin
19 Amendment and what he found in his regression analysis is
20 that, in fact, credit volume decreased by eight percent and
21 debit volume increased by about 16 percent. Exactly the kind
22 of quantitative change you would expect to see if two things
23 were, in fact, constraining one another, if they were
24 competitive. And that's Dr. Katz's regression analysis, not
25 Dr. Bernheim's.

1 I'd like to turn to travel and entertainment and
2 then just a little bit on market power and I'll be done,
3 Your Honor. Travel and entertainment.

4 THE COURT: Go ahead.

5 MR. CHESLER: Four points.

6 First. It appears, Your Honor, to us, admittedly we
7 are advocates so we may be too cynical, but it appears this
8 was a litigation-driven strategy because it was a way for the
9 Government to put something up on the board in which
10 American Express had at least 30 percent of some market since
11 no other market floating around here has that kind of a share.

12 And the reason I say that that's what it is, is
13 their rationale for defining this market is price
14 discrimination. Before you ever get to the concession
15 Dr. Katz made that you only find price discrimination if you
16 look at price as compared to cost, if you look at margin,
17 let's just look at even just price for a moment.

18 The record is clear that American Express charges
19 different prices for different industries. It has price
20 schedules, discount rates schedules for different industries.
21 Professor Katz conceded that if you're going to define a
22 market based upon the fact that American Express rates to T&E
23 merchants are different from their rates to everyday spend
24 merchants, then every industry could sustain a separate market
25 definition because the rates are different for each industry.

1 So, why didn't they have a fast food market? Why
2 didn't they have an airline that goes interstate or
3 international market? Why didn't they have a market for
4 restaurants where the bill is going to be over a hundred
5 dollars for dinner? Because they wanted a market that had
6 over 30 percent. Because the principle, the principle doesn't
7 make any sense here. The principle would define 100 different
8 markets because they charge a different rate to each industry.

9 Second. Professor Katz admitted that you need to
10 look at cost. Price minus cost tells you whether you're
11 discriminating because you're getting different rates of
12 return for different industries. The Government's proposed
13 findings on this issue appear at numbers 626 to 632 of their
14 submission. There is not the word cost once in those
15 findings. Not once.

16 Professor Katz said you've got to look at the
17 margins. And when I asked him that when his SSNIP test wasn't
18 it true that according to his analysis American Express earned
19 the same gross margin in T&E and non-T&E, 17 percent, he said
20 yes. His calculations came out to the same margin.

21 So, he didn't accept a proposition that different
22 prices means different markets or he'd have had an armada of
23 different markets. He just aggregated together a bunch for
24 T&E. He accepted the proposition that you have to deduct
25 cost, you have to look at margin, but then I confront him with

1 his margin calculations in the context of SSNIP and show that
2 he's got the same margin for both, yet they hold on to the T&E
3 market.

4 Your Honor, the market makes no sense; not because
5 it couldn't be sustained as a commercial operation, although
6 that's a pretty relevant piece of evidence. The fact that if
7 we had continued to be in our niche, as Visa said, we probably
8 would be in the dirt pile of history by now. But that's not
9 really our point. Our point is that the spillover is so clear
10 here that the market makes no sense as a defensible market.

11 Take the following proposition. I fly after court
12 today to Chicago. I buy a ticket on American Airlines.
13 That's a T&E transaction.

14 I take a cab, I don't know where the cab is, if it's
15 in or it's out, let's leave the cab aside.

16 I get to the hotel, I check into the hotel with my
17 American Express card, T&E transaction.

18 On the way to the elevator, I realize I left my
19 razor and shaving cream at home. I stop in to the newsstand
20 and spend five bucks on a razor and some shaving cream. Is
21 that a T&E transaction? I don't know and they haven't told
22 you.

23 I decide I'm hungry, I want a snack. I go down the
24 street to McDonald's and I buy a Big Mac. Their Exhibit that
25 they showed you today had McDonald's, Wendy's, Burger King.

1 They're all T&E merchants according to the Government.

2 They told you that the problem, the reason we have
3 power in the T&E market as they call it, is that those vendors
4 have to do business with us because we have 70 percent of
5 corporate cards and we have a lot of market power, but they
6 have Wendy's and Burger King in the market. Are they honestly
7 telling you our corporate cards give us power with Wendy's and
8 Burger King?

9 So, you might say that makes no sense, I'll chop
10 them out. Where do you stop chopping? They haven't told you
11 where. They've got Subway Sandwiches in there, too. Are they
12 in or are they out? I don't know. They haven't proven the
13 market.

14 I've been doing this for 37 years, 38 years, I've
15 defended a lot of companies in a lot of antitrust cases. The
16 plaintiff always tells you exactly who's in the market. They
17 have not only not told you, they've given you no set of rules
18 so you can figure it out. The market, Your Honor, makes no
19 sense and the spillover effect is fatal to the market. And
20 city pair analysis doesn't work, Your Honor. It doesn't work
21 because of spillover.

22 The analogy just doesn't work. If you fly from
23 New York to Chicago and that's a city pair, you fly from
24 New York to Chicago. Our point is while you you're sitting at
25 the airport you buy a New York Times and you buy a chocolate

1 donut, if you can't use your American Express card for that
2 trip -- you might have left it home in your chest of drawers,
3 you might just stick it back in your pocket -- you can't use
4 it, you're going to use one card for the trip, that's
5 spillover and it's not speculation. It's a real fact and it's
6 all over this record. That's why the T&E market makes no
7 sense.

8 Let me turn to market power, Your Honor.

9 I don't think even the Government says it's not
10 important, they simply say they can solve the problem of
11 market power by their alternative theory of anticompetitive
12 effects. Well, I've spent a lot of time on effect, so I'm not
13 going to go back there. So, let me look at the power
14 evidence-qua-power evidence. Because they say that they've
15 also proven their case the old-fashioned way.

16 Well, why is it so important? First. It's
17 important, Your Honor, because you asked this question
18 actually at an earlier conference before the trial and it may
19 have been at the summary judgment argument. You asked both of
20 us how am I supposed to go anecdotal evidence of what
21 individual witnesses say to get to what is true of the
22 marketplace? How am I supposed to get there? Great question
23 and it's a daunting task.

24 Here, my point is this. The reason that market
25 power is so important even if the Government tries to go the

1 shortcut route of anticompetitive effects, and even assuming
2 contrary to what I've said before they actually had proven
3 actual adverse effects -- which they haven't -- how do you
4 know that you can extrapolate from the examples they've given
5 you to an anticompetitive effect in the marketplace?

6 Well, one sanity check on that is to look at the
7 evidence of power because everyone I think agrees, and
8 Professor Katz admitted, that a company that does not have
9 market power, in fact, cannot be expected to visit
10 anticompetitive effects to the market through its conduct that
11 the antitrust laws should care about. So, one sanity check on
12 whether the anecdotal evidence is good or not is looking at
13 the separate evidence of power or not.

14 So, what is the separate evidence of power?

15 First, I said this before but it bears repeating in
16 this context, the reason the Government says they're not suing
17 Discover is because Discover has a low share. Share matters.
18 Share suggests whether you can or you can't harm. So, what
19 are the metrics here?

20 Slide 74, cards in force. We're last. Last. And
21 by the way, in the Visa case, which the Government doesn't
22 like me quoting from, the Government stated if you're not
23 ubiquitous, you can't be a viable competitor in this market.
24 I can cite that quote to you in a few moments. 53 million
25 card versus 254, 178. You heard testimony over and over again

1 to many merchants we're not relevant because no one shows up
2 with our card. We're last in a field of four.

3 Transactions, slide 75. 17 percent. Visa and
4 MasterCard have over 70 percent of the transactions involved.
5 That's not dollars, Your Honor. That's the number of
6 transactions, 17 percent.

7 Slide 76, merchants in locations in force. We've
8 seen this chart many times before. We're at about two thirds
9 of the others. A full third of the merchants who accept their
10 card do not accept ours. That's the experiment I talked
11 about.

12 Slide 77. Charge volume, 26 percent. Visa's
13 got 45 percent. MasterCard almost the same percentage as ours
14 and as I said, they don't compete with each other in the real
15 world. Combined, they're about 70 percent and that's without
16 debit in the market. If you put debit in, our share goes down
17 to 13.9.

18 Now, the Government says well, MasterCard was found
19 to have power in the U.S. v. Visa case with a comparable
20 share. Well, when MasterCard argued in that case that they
21 couldn't be found to have power because they were only five
22 percentage points different from Amex, which was held up as
23 the poster child of a victim by the Government in that case,
24 the Government said that's a red-herring, a phrase that
25 Mr. Conrath used this morning in a different on text. The

1 Government said that's a red-herring.

2 That's a red-herring because, in that case,
3 MasterCard was jointly owned by the same banks as Visa. The
4 relevant comparison is MasterCard then versus Amex now. And
5 what the Government said was you can't compare the MasterCard
6 share to the American Express share because they're commonly
7 owned with Visa, they're controlled by the banks, they're
8 accepted at virtually every merchant in America, they've got
9 multiple numbers of the cards in force as compared to
10 American Express. They were citing exactly the same metrics
11 then to argue the opposite side of the same issue that they're
12 arguing now, and now they're backhanding the metrics. They
13 don't matter. The Government can't explain that 180. They
14 don't try. It's not in their papers because they don't have
15 an explanation.

16 The law in the Second Circuit, Your Honor, is if, in
17 fact, you have less than a 30 percent share, there is a
18 presumption that you lack power. It's not a rebuttal. It's a
19 presumption. Judge McMahon in the Commercial Data Servers
20 versus IBM case says that. She cites a bunch of Second
21 Circuit cases and elsewhere for the proposition. You've got
22 to come forward with substantial evidence to overcome that
23 presumption.

24 But for the MasterCard example, which as I said is
25 dramatically different, they have no other examples. Case

1 after case after case with shares this low say no, no power.
2 No power. Not to mention all the other metrics, which are
3 also lower.

4 So, the Government also says that it's Amex's choice
5 that it's smaller, so we shouldn't get any benefit from being
6 smaller having many fewer locations accepting us, it's a
7 self-inflicted wound. Quagliata, Pojero, Chenault, Gilligan.
8 They came in here one after another after another saying it's
9 a huge deficit for us. It's the most common argument that
10 companies use against us when bidding for their corporate card
11 business, that our acceptance is lower.

12 Silverman came in and talked about the problem of
13 active merchants versus inactive merchants and having so many
14 in San Francisco that are inactive. About being in Montana
15 and being unable essentially to find any merchants that accept
16 your card. That these are big problems if you go on a
17 vacation and you have your Amex card. It simply strains
18 credibility, Your Honor, to suggest that American Express is
19 happily sitting back in fourth place because it wants to.

20 It is inconsistent with the sworn testimony of all
21 of those executives that they've tried zero discount rate
22 proposal, they have tried all sorts of techniques, they've got
23 intermediaries out now trying to sign up merchants to fill the
24 gap and despite all their efforts the gap grows because the
25 others are signing more merchants. The idea that they're

1 sitting back voluntarily and doing that is simply inconsistent
2 with the record.

3 Let me turn, Your Honor, to the other evidence about
4 power. Pricing.

5 Well, if share doesn't work, what else do you do?
6 Well, you could try looking at price. I said before the
7 Government says our price is too high, but they haven't proved
8 what the competitive level is so they can't say they're super
9 competitive. They can only say they're higher.

10 Second. On a mixed basis, they're not higher. The
11 premium is gone and that testimony is unrebutted.

12 Their expert said economic profits are the right
13 measure. They used accounting profits. The cases are quite
14 clear and the economic literature is quite clear that in an
15 antitrust case the proper measure if you're trying to prove
16 financial basis for power, use economic profits. They didn't
17 do that.

18 They point to our filings with the SEC and they say
19 look, American Express has profits. Well, if having profits
20 was enough, then virtually every company in the Dow and many
21 more who aren't in the Dow would have antitrust power,
22 monopoly power, market power. Because they're profitable.
23 Obviously, that's not the standard, Your Honor, and it
24 shouldn't be suggested that it is.

25 So, they just don't have a pricing basis and when

1 they talk about margins, the only margins they refer to are
2 accounting margins again. And when they made the suggestion
3 to Mr. Silverman well, if you make four billion bucks, why
4 don't you just take a billion off the table and lower your
5 rates to the merchants by a million dollars, you'd still make
6 three, he explained to them, a little tutorial can't on the
7 way public corporations work. Your investors stay with you if
8 you get an adequate return on investment and they leave if
9 they don't.

10 And American Express has made the judgment that they
11 can't do that for two reasons. One, it would kill the return
12 on investment to their investors and two, if they took that
13 kind of financing out of this circle that they're in, of this
14 business model that they're in, then their product
15 differentiation recedes, the insistence and loyalty of the
16 customers as Dr. Katz admitted evaporates, you remember his
17 dog food analogy, and they become an undifferentiated product
18 in a market dominated by the other two networks.

19 So the Government's suggestion of how American
20 Express should run its business, with respect, doesn't work
21 and the people who actually run its business explained to the
22 Court and to the Government why it doesn't work.

23 With respect to the efforts to acquire merchants
24 Your Honor, just a few examples.

25 Safeway. They had to take a test. Do you remember,

1 they did a test out in Hawaii to show that they were worthy of
2 being accepted by Safeway and they flunked the test? And
3 Mr. Pojero said well, I think maybe we screwed up the way we
4 structured the test, but we won. So, what did they do? They
5 had to pay a huge signing bonus to get Safeway. That's not
6 evidence of a company with the kind of power that violates the
7 antitrust laws.

8 Publix. It took five to seven years of negotiations
9 to convince Publix to take American Express cards and then we
10 had to pay renewal bonuses to them to stay in the game.

11 GEICO. We sent them one of these insistence
12 letters. We said oh, look what could happen if you stop
13 taking American Express. It took eight months to resolve
14 their cancellation threat. They weren't persuaded by the
15 insistence numbers and, in fact, it was only after we lowered
16 their net effective discount rate and an independent actuarial
17 firm came in and confirmed that Amex was delivering more value
18 to them than the bank card were that GEICO agreed to renew.

19 We've got evidence with respect to Apple, with
20 respect to Target, with respect to Dell and many others,
21 concession after concession after concession to keep and renew
22 merchants. I would submit, Your Honor, that where you need to
23 make a compelling showing, a substantial showing of power,
24 where you haven't proven the anticompetitive effects on their
25 face, that's not a compelling showing of power. It's quite

1 the opposite.

2 Value recapture. Your Honor, one your questions
3 really got to the meat of the batting order. Value recapture
4 is over. If we had power over price and we were rational
5 business people, why would we stop charging merchants more
6 when we could? We stopped for the reasons Mr. Gilligan came
7 in here, sat in that chair and swore under oath were true. He
8 said the pain was greater than the gain.

9 We were destroying our relationships with merchants.
10 He said I personally spoke to the Continental people. They
11 told me how angry they were over value recapture. Now
12 Mr. Conrath said oh, but there's a contemporaneous document
13 that says it's the Chase relationship. Well, I went back and
14 looked at the document while Mr. Conrath was speaking and, in
15 fact, the document goes on for two pages and it discusses two
16 things.

17 It says we have an arrangement with Chase which
18 would make it difficult for to us continue. Not impossible,
19 difficult. And then it says and you guys are saying we're
20 hostile to you? We're putting up signs in our lounges saying
21 that after a certain date we're no longer going to take Amex?
22 If you want to see hostility, Mr. Gilligan, look at what your
23 own team is doing. You pushed through a \$12 or \$13 million
24 rate increase -- that's value recapture -- and then you went
25 to pay with points so that if you use points your customers

1 could pay their bills for our airline and you didn't so much
2 as give us a telephone call. That's hostility, he said.

3 Mr. Conrath didn't tell you about the back half of the memo.

4 Most importantly, Mr. Gilligan swore to this Court
5 that he personally killed the value recapture program because
6 of the damage it was doing to the merchants. If he could get
7 away with it and they had no choice and they were the
8 prisoners of war that the Government would have you to
9 believe, they wouldn't have had to do that. They did it
10 because they had to.

11 Now, with respect to price on value recapture.
12 Mr. Conrath spent a fair amount of time repeating what
13 Dr. Katz said.

14 THE COURT: Can I just ask you about value
15 recapture?

16 MR. CHESLER: Yes, sir.

17 THE COURT: If it was such a terrible idea, who in
18 his right mind would even propose an idea like that at a
19 sophisticated corporation like American Express unless that
20 individual or that group that approved it, thought that they
21 could do exactly what you said they couldn't do.

22 MR. CHESLER: Right and I will explain it because
23 it's what the record shows.

24 THE COURT: Oh.

25 MR. CHESLER: Here's what the evidence shows. Ten

1 years of virtually no rate increases, almost none at a whole
2 wide swath of merchants.

3 Costs for rewards going up. Redemptions are
4 skyrocketing through the roof. Rates have remained the same.
5 Without the benefit of the rearview mirror, the analysis was
6 well, they're getting more value, we're driving demand at
7 these merchants because we're reserving more and more money to
8 pay for those rewards, those rewards only get redeemed when
9 they actually use the card at these merchants, we're
10 delivering buyers to these merchants, but we're not raising
11 our rates. So, we think we can raise our rates to do exactly
12 what the name suggested. Recapture value that we were
13 providing to the merchants which we weren't capturing because,
14 unlike most products I'm familiar with, the rates hadn't
15 changed in a decade.

16 With the benefit of hindsight, Your Honor, not
17 foresight, you heard what Mr. Gilligan said. It got a lot of
18 people very angry. It was more harm than good. I killed it.
19 If he had known that was going to happen at the beginning, I
20 completely agree with you, why would anybody have done that?
21 But the record shows they didn't. They thought they could get
22 more money for the value they were providing and that they
23 were charging lesser price than they were entitled to. They
24 got some, they didn't get others and then they got a lot of
25 people angry.

1 By the way, as everybody admitted, it didn't reverse
2 the decline in the discount rates. It slowed the rate of the
3 decline. Over time the discount rates continued to decline,
4 notwithstanding value recapture and it was stopped four years
5 ago.

6 Your Honor, even if you write it off as evidence of
7 a dumb idea, I submit to you it's not evidence of antitrust
8 market power. That's not a story consistent and I haven't
9 seen any case law that they've cited that has stories that end
10 that way in which the Court says yup, that looks like power
11 over price to me. I haven't seen them.

12 So, Your Honor, that leaves one other issue about
13 power, which Mr. Chenault didn't really directly mention. He
14 mentioned it by implication and that's insistence. I just
15 want to spend a moment on insistence.

16 In the Visa case the Court says, and Mr. Conrath put
17 up a chart that had what he called the road map to prove
18 power, one of which was customers are insistent in the Visa
19 case. And as I said to Your Honor in the opening and I just
20 remind you of this, insistence that's driven by investing in
21 consumer benefits is not the same thing as insistence that's
22 driven by necessity.

23 If you are a merchant who wants to accept plastic
24 transactions in this country, you must carry Visa and
25 MasterCard. That's why that bar was nine-point-some million

1 merchants and we're at six. Whatever the Government's
2 theories may be for why there are three-plus million locations
3 that don't carry us, the fact is they don't carry us and they
4 must think they're doing just fine without us or they would
5 carry us.

6 They haven't told you about more than a handful of
7 merchants that are on a cash only or check only basis.
8 Virtually all of them accept plastic and if you accept
9 plastic, you accept Visa and MasterCard. That's a utility.
10 That kind of insistence is evidence of market power and the
11 Second Circuit was correct to observe it.

12 Insistence that's born out of a continuous
13 investment, as their own experts testified, if the rewards
14 went down, the loyalty would go down. If you stop providing a
15 really high level of benefits to your consumer, I would expect
16 to see their share of spend decline, is what he said. I would
17 expect to see a drop-off in the insistence of the customers.
18 That's not market power. Whatever word you want to use, it's
19 not antitrust market power. And it's certainly not analogous
20 to what was the case in the Visa and MasterCard case. It
21 simply isn't.

22 Now, the Government says well, small merchants have
23 no choice. They also say, as I said before, they're not
24 benefitting at all from the Visa-MasterCard decree. In fact,
25 I think they said Visa and MasterCard, Dr. Katz said they

1 won't even talk to the small merchants, so I'm not surprised
2 that nothing's happened. Well, then this case must come down
3 to a case for the two percent of the merchants. If
4 the 98 percent are somehow captives and nothing's going to
5 help them, then this is a case for the two percent.

6 Every single witness the Government called as a
7 merchant witness is in that two percent. And as Your Honor
8 said the other day in the fairness hearing on the settlement,
9 you know, there's an issue about the leverage that those
10 merchants have to negotiate with American Express. That
11 leverage was displayed from that witness stand over and over
12 and over again. Apparently the Government's new theory is
13 that they brought the lawsuit just for them because
14 the 98 percent are beyond help. That doesn't make much sense.

15 And by the way, when they point to the small
16 merchants we called, they misstate the record. They refer to
17 Strictly Bicycles, Mr. Gutierrez that had the bike shop over
18 near the George Washington Bridge, remember him? They cite
19 him in their finding of fact 163.

20 They say well, even he said he wouldn't drop
21 American Express. Well, what did he actually say? He said I
22 won't drop American Express because they are a really good
23 partner, they are valuable to me. They gave me a business
24 loan. I was able to buy property next to my store when I
25 couldn't get a bank loan. That part got left out of the

1 finding.

2 Small merchants matter. As I said before, the
3 millions who don't carry us are the same size as the
4 98 percent of those who do.

5

6 (Continued on following page.)

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1 MR. CHESLER: In conclusion, Your Honor, by the case
2 law, with durability, we cite it in our papers, it has to be
3 durable power in order to be antitrust power.

4 So, in conclusion, what to say about the
5 government's "but for" world. It's a world which according to
6 Dr. Katz is one in which merchant discount rates might go up,
7 not down, in which the quality of the product, the
8 differentiation of the product might go down, not up, in which
9 merchants would be free to discriminate in almost any way they
10 wish. The only limitation appears to be you can't
11 affirmatively disparage the product, but as we demonstrated in
12 the evidence at trial, we can say things like the welfare of
13 my family depends upon you not using that card, please, please
14 don't do this to my family. There's nothing in the
15 government's case that suggests people couldn't do that. And
16 more, American Express can't do anything about it.

17 We can't even say if you, merchant, are standing
18 between me and the consumer who carries my card and every
19 single consumer with my card who walks into your store is met
20 with that kind of a hostile reception, I'm stuck. I have to
21 stay in business with you because if I terminate you, then
22 according to the government, I'm through the back door doing
23 what their proposed injunction would prevent me to do from the
24 front door.

25 I can't find any precedent for that, Your Honor, any

1 precedent for the proposition that a seller of a product must
2 submit to that kind of discrimination against its product by
3 the vendors, the intermediaries with whom it does business who
4 sit between it and the ultimate consumer and is powerless to
5 do anything about it. More importantly, that the antitrust
6 laws require that result.

7 Now, they can cite you a lot of cases that say they
8 foster competition and a lot of general platitudes of the
9 purpose of the law, but that kind of blatant discrimination
10 that injures somebody's business and they can't even walk away
11 would be unprecedented.

12 And insistence won't stop the process because as the
13 steering takes place and as the funds for funding the rewards
14 go down, the rewards will go down and as Dr. Katz admitted as
15 the rewards recede, so too will the loyalty of the customers.
16 And that's what we saw, not I, I wasn't there, but that's what
17 Mr. Chenault and his colleagues saw in the '90s, in the We
18 Prefer campaign. That's precisely what they lived through.

19 So, the government has not satisfied the correct
20 legal standard. Instead, they moved or attempted to move the
21 goal post in to the wrong standard.

22 And I submit, Your Honor, that American Express is
23 today exactly what it was when the government sued Visa and
24 MasterCard and called Mr. Chenault to the stand. It was the
25 best hope in the market, not Discover which barely shows up in

1 the internal documents of Visa and MasterCard, and by their
2 own admission, can't move anything anywhere and which didn't
3 do exactly what they say it would do if it had the opportunity
4 when it had the opportunity over the past three or four years.
5 Discover is not the answer. And for them to put their eggs in
6 the Discover basket and attack American Express as a
7 competitor, given what they did 14 years ago is pretty
8 stunning.

9 This is not a case about protecting American
10 Express. It's a case about protecting competition and,
11 therefore, Your Honor, with all respect, we ask that you enter
12 judgment in favor of American Express and against the
13 government's case.

14 Thank you very much.

15 THE COURT: Thank you. Let me just ask you a
16 question.

17 MR. CHESLER: Yes.

18 THE COURT: Just for the sake of this discussion,
19 you sort of dipped into the remedy department very adroitly in
20 your last three sentences.

21 MR. CHESLER: Thank you, Your Honor.

22 THE COURT: Well, but I caught it.

23 MR. CHESLER: Yes, you did.

24 THE COURT: And you gave the parade of horrors
25 remedy that might be imposed, let's say.

1 Is there something short, were there to be a finding
2 of a Sherman Act Section 1 violation, is there something short
3 of that extreme remedy that you sort of posted to me just now?

4 Is there anything in between the parade of horrors
5 and the NDPs?

6 MR. CHESLER: Your Honor, the honest answer to that
7 is I don't know. We have not spent time trying to construct
8 alternative remedies because we have been focused on the
9 merits of why we think no remedy is required. The only remedy
10 we've ever heard about or seen from the government is the Visa
11 MasterCard remedy so I have no idea. I don't believe so.

12 THE COURT: You understand why I'm asking. I mean,
13 you sort of posed --

14 MR. CHESLER: Right.

15 THE COURT: -- the parade of horrors remedy that you
16 think is appropriate for all the reasons you stated because
17 you don't think there's liability and, you know, I understand
18 your position, but I'm just trying to get a sense of at what
19 point, should that ever happen, would we come back and talk
20 about appropriate remedies once, if there were a finding
21 liability.

22 I haven't concentrated on remedies either because
23 I'm concentrating on liability.

24 MR. CHESLER: Good.

25 THE COURT: But I'm just wondering whether that's,

1 we would save that for another day and another proceeding.

2 MR. CHESLER: I understand. Substantively, my
3 answer is I doubt it but I honestly don't know because as I
4 said, we've been focused entirely on liability.

5 Procedurally, Your Honor, the one thing I would cite
6 to you is the history of the U.S. v. Microsoft case where I
7 believe the trial court did not hold separate proceedings
8 vis-a-vis remedy before entering an injunction. That went up
9 to the DC Circuit and if I have my history correct, and I'm
10 doing this from memory, I believe the DC Circuit vacated the
11 remedy and sent it back and said there had to be separate
12 evidentiary proceedings with respect to the remedy.

13 THE COURT: There was Judge Cote in the Apple case
14 too.

15 MR. CHESLER: That may well be.

16 THE COURT: Where she, step one was liability and
17 then they came back and discussed --

18 MR. CHESLER: I was just thinking Judge Cotark --

19 THE COURT: Judge Kotelly. I know Judge Kotelly,
20 yes.

21 MR. CHESLER: That's one example that comes to mind
22 procedurally in answering your question.

23 THE COURT: And, I mean, the procedural solution
24 that Judge Cote utilized is another example of taking the
25 matter one step at a time, but thank you.

1 MR. CHESLER: I believe that's right. Thank you,
2 Your Honor, very much.

3 THE COURT: Thank you very much.

4 Mr. Conrath?

5 MR. CONRATH: I would like to do a brief rebuttal.

6 THE COURT: Do you want a couple of minutes?

7 MR. CONRATH: I would appreciate a couple of
8 minutes.

9 THE COURT: Very good. We will take a ten-minute
10 break.

11 MR. CONRATH: Thank you.

12 THE COURT: Thank you.

13 (Court is in recess.)

14 (The following occurred in open court.)

15 THE COURT: All right. Please be seated.

16 Mr. Conrath?

17 MR. CONRATH: I will be brief, Your Honor.

18 THE COURT: Okay. Go ahead.

19 MR. CONRATH: So I will be brief because I believe
20 almost all the issues that we've discussed with you today are
21 covered in our papers. I'll try to highlight maybe a few that
22 can benefit from additional comment, but I won't belabor this.

23 THE COURT: All right. Fine.

24 MR. CONRATH: So I'm going to go through, just touch
25 on a few topics.

1 The first topic is the question of issuer
2 competition. We heard a lot of arguments, the substance of
3 which was look at all this competition among issuers to issue
4 cards and pay no attention to that suppression of competition
5 over here for merchants.

6 And as I think we've said, that's inappropriate but
7 I just like to read the portion from the District Court
8 opinion in U.S. v. Visa because a very parallel argument was
9 made there. This is at page 330.

10 The defendants argue strenuously that no consumer
11 harm results from the exclusionary rules because the member
12 banks of the associations compete fiercely as card issuers
13 with each other and with American Express and Discover to
14 offer lower interest rates and all manner of incentive
15 programs to card consumers. This issuer level of competition,
16 however, does not take the place of competition at the network
17 level.

18 And I submit, Your Honor, that same principle
19 applies here. There's a lot of competition on issuers. No
20 dispute about that. It doesn't answer the question about the
21 restriction of competition here.

22 In U.S. v. Visa, let's remember what happened. A
23 restriction was removed and that, the restriction on
24 competition for, among networks for issuers. That did
25 increase that competition. That restriction was on the other

1 side of the, of the network platform. Get rid of the
2 restriction that exists on this side of the network platform,
3 a similar thing will happen. There will be additional
4 competition and that's what we're asking the Court to do in
5 this case.

6 The second area of topics I'd like to talk about
7 involves price effect. We've proved both harm to the
8 competitive process, disruption of that essential connection
9 between cutting your prices and increasing your business in
10 the words of the Supreme Court.

11 Indiana Federation stands for two principles that
12 are relevant and I just want to go back to that. The first is
13 that a finding of actual sustained effects on adverse effects
14 on competition can be legally sufficient to support a finding
15 that the restraint was unreasonable, even in the absence of
16 elaborate market analysis. That's one proposition. The
17 second one is that process harm is a direct effect. If
18 there's conduct that is likely enough to disrupt the proper
19 functioning of a price setting mechanism in the market may be
20 condemned even absent proof that it resulted in higher prices
21 or, as here, the virtues of higher price services than would
22 incur in its absence.

23 Just stepping back in the Indiana Federation for a
24 moment and thinking about the bigger picture, what that was a
25 majority of dentists in two counties in Indiana said we're not

1 going to give the insurance companies x-rays. The court said
2 that was clear enough interference with the price setting
3 mechanism that it can be found unlawful.

4 Look what we found here after a six-week trial. The
5 most direct form of price competition, the kind that's likely
6 to work for merchants has been impeded because, and has cut
7 the connection on what the Supreme Court has said is the
8 essence of competition, cutting price to increase your
9 business. This is a much stronger case when you think about
10 it for finding a harm to the competitive process. But that
11 doesn't matter, really, it doesn't have to matter because
12 there's evidence, direct evidence of price effect here.

13 There was price of competition. It was suppressed.
14 The single clearest case is watching that line of prices go up
15 in Discover's chart. There were low prices. They couldn't
16 succeed in the market because of the anti-steering rules and
17 prices increased. That is direct evidence of a price effect.
18 By itself, it's sufficient. It happened in the past.
19 Mr. Hochschild said if I had the chance, I'd do it again.
20 That ought to be enough to meet our burden whatever the
21 standard is.

22 Now, there was some questions about what
23 Professor Katz said about price. So we heard -- I think the
24 Court saw Professor Katz and --

25 THE COURT: I definitely saw him.

1 MR. CONRATH: Yes.

2 THE COURT: Is this a test? Go on.

3 MR. CONRATH: And maybe "observed" is the right word
4 that I'm looking for because you probably observed that if you
5 asked Professor Katz a direct question, you are going to get a
6 direct answer.

7 He was asked, is it possible, if we removed these
8 restraints, is it possible that price could go up and he
9 answered, as he must, yeah, it's possible. He is explaining
10 that the principle of the antitrust laws is that the antitrust
11 laws don't tell you what prices have to be, what products have
12 to be offered. The principle is let competition decide. Let
13 the market decide. Yes, it's possible if you remove the
14 restraints, you know, AMEX might decide they're better off as
15 a super premium card. Maybe that involves higher prices.
16 There is evidence that there will be competition to increase
17 rewards possibly.

18 What's the overwhelming weight of the evidence? So,
19 there wasn't a follow-up question to Dr. Katz, well, what do
20 you think, what in your professional opinion is probable, but
21 he testified about that extensively. His professional opinion
22 is that what's probable is prices will be lower if there is
23 more competition and he explained why that is extensively and
24 that's more than sufficient evidence to reflect the fact that
25 there's been harm to, to competition in the form of increased

1 prices in this market.

2 THE COURT: Well, let me ask you this.

3 Let's assume that Mr. Chenault is right, all right,
4 and we go to the extreme here and the NDPs go away and there's
5 competition in the marketplace and American Express can't find
6 a business model that is viable in competition with Visa and
7 MasterCard, the grand duopoly of the plastic world. All
8 right? And American Express disappears from true, a true
9 competitive posture with the duopoly.

10 Now, the duopoly is out there alone. There is no
11 competition. They get to do basically what they do either
12 because they know that they can both do it or because they
13 know each other's modus operandi and they figure they're both
14 going in the same direction, you know, they're rocketing up to
15 more expensive discount rates.

16 How does that square with your objective to promote,
17 in the Justice Department, to promote competition?

18 MR. CONRATH: Okay. May I take that in two parts?

19 THE COURT: Sure.

20 MR. CONRATH: One, the first part is that that --
21 and I understand why American Express is making that argument.
22 I can't tell you how many times I've heard the argument that
23 the world will end if we can't continue this particular
24 anti-competitive restraint. With all respect, it's very
25 unlikely.

1 American Express is the largest issuer of cards in
2 the country. It has about, I think, a 25 percent share in the
3 card issuing market. Remember, American Express is in the
4 issuing market as well as the network market.

5 THE COURT: I understand. You all have taught me
6 about the issuing market. It reminds me of that other subject
7 I don't even want to say.

8 MR. CHESLER: Does it begin with a "D"?

9 THE COURT: I don't know what you're talking about.
10 Go ahead.

11 MR. CONRATH: All right. There -- I believe the
12 second largest is perhaps Chase which is about 20 percent so
13 they are in a very favorable position in the issuing market
14 which, of course, is very important for them. They --

15 THE COURT: But do you really -- let me ask you this
16 as a practical matter. As compared to just Chase --

17 MR. CONRATH: Yes.

18 THE COURT: -- Chase's reach is so extensive. They
19 could easily bypass American Express in the issuing market and
20 they are certainly aggressively attempting to do that if the,
21 if my mailbox is any, is any indication. All right?

22 If American Express loses this case, wouldn't that
23 make it more likely that it would be less able to compete in
24 the issuing market or should I care about that from a legal
25 standpoint?

1 MR. CONRATH: Well, that's the second part of my
2 question.

3 THE COURT: Go ahead.

4 MR. CONRATH: But I was resisting getting to it
5 until I talked about the first part.

6 THE COURT: Go ahead. Continue.

7 MR. CONRATH: Okay. But the answer is the antitrust
8 law doesn't protect competitors, they protect competition is
9 the second question, but let me go back to the first point and
10 answer it.

11 Could Chase easily overtake American Express? Well,
12 if it was easy, why don't they do it today? All right.
13 American Express -- so American Express has a lot of
14 advantages for competition. Just think about it. I mean,
15 they're not -- we're not here to protect them, the laws are
16 not to protect them, but just to think realistically because
17 they're making an important argument which is, say, look, this
18 is going to be terrible for us. I think we have to evaluate
19 that critically and think about how realistic that claim is.

20 They have 25 percent share in the issuing market.
21 They have a base of very loyal cardholders. They have a very,
22 very prominent and valuable brand name. I won't recall
23 exactly, but more valuable than Visa, more valuable than
24 MasterCard.

25 THE COURT: It's in the record.

1 MR. CONRATH: It's in the record. Almost everything
2 we say is probably in the record.

3 They have a very talented of employees. I mean,
4 we're -- you saw a lot of their employees there. They're a
5 talented group. They have a lot of resources and they have a
6 very wide merchant network covering more than 90 percent of
7 the credit card spend. So they have a lot of competitive
8 assets.

9 So the question, a question is would a change in the
10 anti-steering rules make it impossible for them to continue to
11 use those assets to succeed in the marketplace or, or to be in
12 the marketplace because, let's face it, I think nobody would
13 say, well, they're entitled to their same current level of
14 success. That's about what their argument amounts to. They
15 say, we've achieved this, we're entitled to maintain our
16 current position, anything that's going to badger us will spin
17 us over the cliff.

18 (Continued on next page.)
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1 MR. CONRATH: If you look back at the history of the
2 20 years of market share, they have been up and down but not a
3 lot. It's I think from nineteen to twenty-six percent. So
4 they haven't been at the bottom and there have been variations
5 and there has been competition. You have to expect that if
6 the antisteering rules are removed they will face more
7 competition. But they have been able to succeed by making a
8 package that appeals to cardholders. They have some services
9 to merchants as well. But they have always been the
10 high-price card to merchants and perceived as such. If they
11 have to offer somewhat lower prices to merchants in order to
12 maintain their position they are a very competitive and
13 thoughtful company. They are going to do that. You heard
14 Mr. Funda's testimony. We would be fighting for the business
15 every day with more incentives for our cardholders and with
16 more lower prices for merchants.

17 Now, that does put them in the position that they
18 have to think about, Well, are we going to have exactly the
19 same level of profits that we've always had? If there's
20 anything they are not guaranteed, it's that. It's clear that
21 they are not.

22 So you know looking at the reality of the
23 marketplace, will they face some competitive challenges? Yes.
24 But what is it we think that Chase might do that might drive
25 American Express out? I mean if they offer additional

1 rewards, well, American Express can offer additional rewards.
2 That's what Chase has been doing, the two of them, and others
3 are competing in that vein. If they offer lower prices to
4 merchants, that's true, too.

5 So let's go to the second half of the question.
6 Maybe there are two parts of it. I think the first thing I
7 want to say is you know the premise is I think overstated.
8 American Express has a lot of competitive assets it can bring
9 to bear. The second part of that is, Well, would that lead to
10 a world in which American Express is just gone and Visa and
11 MasterCard are left? That's not an attractive proposition.
12 But we have to ask the question from an antitrust perspective
13 and it's putting -- you put a harsh question to me, your
14 Honor. Let's give the most direct answer. What is it that we
15 think Visa and MasterCard would do that would be bad if they
16 face less competition? Well, raise prices, offer less
17 quality. What's been happening with the antisteering rules in
18 place, raising prices, not just American Express but Visa and
19 MasterCard, prices are in the one way ratchet up.

20 Why is that? Because it's nobody's business
21 strategy to be the cheaper guy. Perfectly rational for
22 everyone who is in the marketplace today. Don't try to be the
23 cheaper guy because it doesn't get you anything. So what's
24 the solution? Is get rid of the thing that is standing in the
25 way of their being a reward for the cheaper guy and let all

1 the card networks compete to see who can succeed in all
2 aspects of the market. Let's be attractive and cheap to
3 merchants, efficient to merchants. Give them quick turn
4 around payments. Be attractive to cardholders. Give them
5 rewards. Give them quick service. Give them low interest
6 rates. Charge low fees. All those are aspects of sustaining
7 yourself in this business.

8 The market we're focused on is the one where the
9 restriction is. You can't benefit from being more efficient
10 and lower priced in that market. That's the one narrow point
11 that we're trying to ask.

12 So, yes, it's harsh to say it but the antitrust laws
13 don't say -- if it were really true that American Express had
14 a business model that was subtracting value from the economy
15 it couldn't sustain itself in the face of competition. The
16 antitrust laws don't say you get to block competition in order
17 to sustain a model that doesn't work. Now, I don't for a
18 moment think that's what's going to happen here. I think they
19 are a very successful and impressive company that has had a
20 lot of success and brings a lot of assets.

21 If you ask me the hard question: Do the antitrust
22 laws protect someone if it turns out they have a business
23 model that just isn't desired by the consumers? You know, the
24 history is littered with companies -- to which the answer is
25 no. It's a harsh answer. I don't think it's relevant in this

1 case. American Express has shown itself to be adaptable.
2 They have adapted through challenges that look a lot more
3 difficult than just we have to face some price competition at
4 the point of sale.

5 THE COURT: And the issue of the relevant market and
6 whether debit fits in the relevant market.

7 MR. CONRATH: The next one on my list.

8 THE COURT: Okay.

9 MR. CONRATH: Let me turn to it.

10 THE COURT: What weight should I put on the
11 Congressional initiative that -- I can't recall the name of it
12 -- that took place recently that established certain
13 regulatory limitations on debit? That one. Should that be
14 significant to me in I guess applying the relevant market or
15 is there something else?

16 MR. CONRATH: I would say the fact that Congress
17 acted should not be. But I love to argue that Congress knows
18 what markets are and you should follow it.

19 THE COURT: You're not going to get an argument from
20 me about that. I just want to know from you whether you think
21 that there's some weight that should be given in the third
22 branch when considering these things, since the antitrust laws
23 are a creation, a legislative creation in and of themselves.

24 MR. CONRATH: I observe that Congress regulated
25 certain changes that related to debit cards and didn't impose

1 the same regulatory changes on credit cards at the same time.
2 I observed that without comment.

3 THE COURT: All right. What were you going to say?

4 MR. CONRATH: And one of them relates to that which
5 is that there was -- the effect of the -- one effect of the
6 Durbin Amendment regulation is a bit of evidence that tells
7 you something, the huge change in prices, very small, if any,
8 reactions. I think there was some discussion of a regression
9 that Professor Katz had and while most of this is in our
10 findings of fact I'm not going to detail the regression
11 analysis. The trial transcript at 4080 to 4081 explains why
12 that evidence, Professor Katz's opinion that tells you that
13 debit and credit are not in the same market. Huge price drop,
14 very small reaction. That's not what you see when two
15 products are in the same market.

16 The bigger point is that what we heard a lot of talk
17 about debit today and what it revealed is that American
18 Express is still asking the wrong question on the question of
19 debit. We agree there are customers who use debit. We agree
20 there are more customers using debit today than there were 20
21 years ago. We agree there are some customers who can switch
22 from debit to credit.

23 AMEX would tell you that that's all you should look
24 at. We have to think about what's the question we're trying
25 to ask. That is a relevant question if you are thinking about

1 your issuing side, like, for example, if you are signing up
2 someone to a Cobrand agreement and thinking about whether
3 there can be an issuer. If I'm a credit card issuer of any
4 kind and I think, A., some people will use debit instead of
5 credit. I have to think about that. We agree with that
6 proposition.

7 The question we are asking is a much narrower
8 question. The question is: Is there a relevant market for
9 merchant network services to merchants? We have to ask, if a
10 hypothetical monopolist put a price increase on merchants what
11 can the merchants do to defeat the price increase? The fact
12 that there are some customers who use both debit and credit
13 does not answer that questions. The answer to that question
14 is: What can the merchant do? The merchant has to ask itself
15 can I switch anybody and Professor Katz explains explained why
16 that's an extremely unprofitable and unlikely strategy.

17 What's left is can I drop credit and rely on debit?
18 And you heard the explanation from the merchants, from
19 Professor Katz, there's a core customers who want to use
20 credit cards. AMEX basically wants to ignore them and focus
21 on the people who use both. But if you are a merchant you
22 don't have that luxury. You have to try to get every customer
23 you can. You certainly can't ignore a big chunk of customers
24 who want to spend with credit or who need to spend with credit
25 that you are going to lose to the competitor down the street

1 who does take credit cards. That's the question that has to
2 be asked in defining a market.

3 We had a lot of talk about how people use credit and
4 how some of those people also use debit. Some people use
5 debit only. All true. That's not the dispute. The right
6 question is: What could merchants do? The answer is it's not
7 practical to substitute acceptance of debit cards for
8 acceptance of credit cards.

9 I wanted to talk briefly about Travel and
10 Entertainment submarket. We heard some discussion about this
11 and the proposition that in theory you could make every
12 industry a separate market and as if that was a surprise. We
13 asked Professor Katz that on direct. It is a common fact
14 about market definition that sometimes you can -- I think a
15 term that Professor Katz used, that there are aggregation
16 markets.

17 You could look at every user of a ball bearings in
18 the country, just to reach into the past antitrust cases.
19 Each one uses a slightly different ball bearing. Is each one
20 a market? Yes, maybe. But it makes sense to talk about them
21 all together and that's what Professor Katz did and he
22 explained clearly the logic of looking both at the broad
23 market and asking one submarket where there's a realistic
24 question of whether there are significantly different
25 conditions and doing the analysis for those.

1 The standard common antitrust tool -- and let's keep
2 in mind that the purpose of market definition is not to
3 obscure reality but to illuminate reality. That's what he's
4 trying to do. What's real market reality here? We can look
5 at the whole thing. Let's see if there's anything special
6 about T&E. That's what that amounts to.

7 And I explained the proposition that a good example
8 here of why you can have an antitrust market even if one firm
9 can't supply it and airline city pairs was the example and we
10 heard back, no, no, that's different because there are no
11 spill-over effects.

12 Well, with all due respect as someone who did spend
13 sometime dealing with the airline industry, there are a lot of
14 spill-over effects in the airline industry. If you are an
15 airline and you have a flight from New York to Houston, that
16 has a huge spill-over effect on your ability to run a
17 profitable flight in Houston as to San Antonio or Houston to
18 Midland. That's an industry that is full of spill-over
19 effects. That's not a distinguishing feature at all. The
20 principle though applies to any kind of industry. There's
21 nothing, no case, no authority, no economic literature that
22 suggests a relevant market should in any way have to be
23 coterminous with a firm being able to supply that whole
24 market.

25 And I think I'll just touch on one other topic which

1 is the last topic you discussed with Mr. Chesler and I think I
2 would say, yes, I think it's appropriate that we get to a
3 remedy phase as the court knows and I think the right way to
4 do it, if we get to remedy, there should be some form of
5 separate proceeding in the form of asking the parties to
6 submit proposals. We're not suggesting that you include that
7 in this opinion, although both sides included some authority
8 on the subject of remedy and in the conclusions of law.

9 The more common practice is to say, all right, we
10 have a liability decision, if we're fortunate enough to need
11 an additional proceeding at that point, you can ask for papers
12 and we'll propose a way to go.

13 With all that, your Honor, unless you have something
14 else for me, thank you for the time. We would like to ask you
15 to find that there's been a violation of section one of the
16 Sherman Act.

17 THE COURT: Thank you very much.

18 With respect to the defense's slides, I'm marking
19 them as Defense Exhibit 1.

20 MR. CHESLER: Thank you, your Honor.

21 THE COURT: On this hearing.

22 Is there anything else from the government?

23 MR. CONRATH: No, your Honor.

24 THE COURT: Anything from the states?

25 MR. GENTILE: No, your Honor.

1 THE COURT: Anything from you, Mr. Chesler?

2 MR. CHESLER: No, your Honor, just the thanks of our
3 entire team for all your courtesies and that of your staff.

4 THE COURT: Thank you to all of you, and we are
5 adjourned.

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I N D E XWITNESSPAGE

SUMMATION

BY MR. CONRATH

6778

SUMMATION

BY MR. CHESLER

6865

REBUTTAL

BY MR. CONRATH

6949

\$	25 [4] - 6800:3, 6868:10, 6955:2, 6956:20 254 [1] - 6930:25 26 [2] - 6823:20, 6931:12 28 [1] - 6901:10 2:00 [1] - 6864:9	6778 [1] - 6968:7 68 [1] - 6802:10 6865 [1] - 6968:9 6949 [1] - 6968:11 6:00 [1] - 6833:23
'90s [2] - 6794:24, 6945:17	3	7
1	3 [6] - 6872:20, 6883:5, 6884:22, 6887:3, 6890:19, 6892:9 3.25 [2] - 6794:25, 6799:25 30 [4] - 6903:24, 6925:10, 6926:6, 6932:17 32 [1] - 6905:9 330 [1] - 6950:9 34 [2] - 6854:16, 6905:18 35 [4] - 6870:4, 6870:10, 6873:13, 6906:13 37 [1] - 6928:14 38 [3] - 6778:19, 6906:22, 6928:14	70 [4] - 6920:23, 6928:4, 6931:4, 6931:15 74 [1] - 6930:20 75 [1] - 6931:3 76 [1] - 6931:7 77 [1] - 6931:12
1 [10] - 6783:9, 6811:12, 6862:13, 6864:1, 6868:18, 6870:3, 6870:8, 6870:9, 6947:2, 6966:19 1,000 [1] - 6910:7 1.3 [1] - 6841:2 1.75 [2] - 6794:25, 6799:25 10,000 [1] - 6903:10 10-CV-4496 [1] - 6772:8 100 [1] - 6926:7 10019 [1] - 6773:12 10022 [1] - 6773:16 10:00 [1] - 6772:18 11-MD-2221 [1] - 6772:15 11201 [1] - 6772:23 12 [3] - 6778:20, 6885:8, 6900:11 120 [1] - 6810:4 13.9 [2] - 6913:1, 6931:17 14 [1] - 6946:7 15 [4] - 6776:9, 6860:11, 6894:15, 6895:1 16 [1] - 6924:21 163 [1] - 6942:19 17 [3] - 6926:19, 6931:3, 6931:6 178 [1] - 6930:25 180 [1] - 6932:13 19 [2] - 6778:19, 6794:21 1993 [1] - 6900:11 1995 [2] - 6875:20, 6899:21	4	8
2	4 [3] - 6883:19, 6884:22, 6893:1 40 [6] - 6813:13, 6813:18, 6813:25, 6814:1, 6828:17, 6869:1 4000 [1] - 6773:3 404 [1] - 6905:10 4080 [1] - 6962:11 4081 [1] - 6962:11 41 [1] - 6831:12 44 [1] - 6838:15 45 [1] - 6931:13 450 [1] - 6773:3 49 [1] - 6840:2	8 [1] - 6892:19 80 [1] - 6893:7 800,000 [1] - 6910:4 825 [1] - 6773:12 85 [1] - 6910:22 850,000 [1] - 6910:7
2 [1] - 6884:18 20 [8] - 6791:16, 6869:7, 6877:9, 6889:21, 6894:10, 6955:12, 6958:2, 6962:20 20/20 [1] - 6796:15 2002 [1] - 6895:4 2006 [1] - 6840:15 2007 [2] - 6840:20, 6905:10 2008 [1] - 6840:24 2009 [1] - 6840:25 2010 [5] - 6804:22, 6840:4, 6840:25, 6841:3, 6895:5 2014 [2] - 6772:17, 6818:12 20530 [1] - 6773:4 220 [1] - 6897:2 225 [1] - 6772:23 24 [1] - 6793:2	5	9
	5 [1] - 6893:1 5.3 [2] - 6910:5, 6910:8 50 [1] - 6912:15 51 [1] - 6913:20 52 [2] - 6851:3, 6913:20 53 [3] - 6851:15, 6913:20, 6930:24 54 [1] - 6914:1 55 [1] - 6918:1 57 [1] - 6919:15 575 [1] - 6773:16 59 [1] - 6854:12	9 [1] - 6772:17 90 [3] - 6799:20, 6800:19, 6957:6 98 [6] - 6884:13, 6884:17, 6884:19, 6942:4, 6942:14, 6943:4
	6	A
	6 [2] - 6892:19, 6893:1 60 [1] - 6922:1 61 [1] - 6922:1 62 [2] - 6856:15, 6922:1 626 [1] - 6926:13 63 [1] - 6923:19 632 [1] - 6926:13 64 [1] - 6923:19 65 [1] - 6923:19 66 [1] - 6924:1	A-1 [1] - 6865:13 a.m [1] - 6772:18 ability [6] - 6792:17, 6792:21, 6862:23, 6886:2, 6905:16, 6965:16 able [24] - 6781:11, 6781:24, 6784:18, 6786:17, 6788:21, 6790:22, 6792:15, 6793:20, 6799:24, 6810:19, 6843:2, 6844:6, 6848:12, 6850:24, 6857:1, 6857:14, 6873:20, 6874:12, 6896:9, 6921:12, 6942:24, 6955:23, 6958:7, 6965:23 absence [5] - 6870:23, 6896:8, 6896:15, 6951:15, 6951:22 absent [1] - 6951:20 absolutely [4] - 6818:14, 6818:15, 6819:18, 6822:9 absolutist [2] - 6913:10, 6913:18 abuse [2] - 6833:25, 6879:22 accelerating [1] - 6918:9 accept [25] - 6810:17, 6819:15, 6825:11, 6835:11, 6835:18, 6837:4, 6837:5, 6853:3, 6872:21, 6881:2, 6883:6, 6883:19, 6884:12, 6884:14, 6926:21, 6931:9, 6931:10, 6933:15, 6940:23, 6941:8, 6941:9 acceptable [1] - 6868:20 acceptance [19] - 6827:17, 6852:8, 6856:5, 6856:7, 6856:8, 6856:19, 6857:9, 6857:16, 6857:22, 6858:12, 6858:14, 6858:19, 6859:5, 6918:25,

<p>6919:11, 6933:11, 6964:7, 6964:8</p> <p>Acceptance [2] - 6902:5, 6902:12</p> <p>accepted [5] - 6838:8, 6906:1, 6926:24, 6932:8, 6936:2</p> <p>accepting [4] - 6820:6, 6835:22, 6852:11, 6933:6</p> <p>access [3] - 6849:9, 6849:11</p> <p>accommodated [1] - 6846:6</p> <p>accommodations [1] - 6846:17</p> <p>according [9] - 6873:15, 6884:19, 6892:17, 6892:23, 6893:1, 6926:18, 6928:1, 6944:5, 6944:22</p> <p>account [4] - 6829:14, 6911:2, 6915:7, 6915:13</p> <p>accounting [2] - 6934:13, 6935:2</p> <p>accuse [2] - 6829:17, 6879:20</p> <p>achieved [1] - 6957:15</p> <p>acknowledged [1] - 6798:15</p> <p>acquire [1] - 6935:23</p> <p>acquirer [4] - 6805:1, 6805:16, 6805:18, 6820:1</p> <p>acquirers [3] - 6805:21, 6805:23, 6921:13</p> <p>Act [7] - 6808:2, 6810:4, 6864:2, 6868:18, 6871:5, 6947:2, 6966:16</p> <p>act [3] - 6790:17, 6825:13, 6893:18</p> <p>acted [1] - 6961:17</p> <p>acting [1] - 6843:11</p> <p>action [1] - 6923:24</p> <p>actions [1] - 6899:23</p> <p>active [1] - 6933:13</p> <p>actively [1] - 6868:2</p> <p>activity [1] - 6831:9</p> <p>actual [22] - 6786:6, 6801:19, 6869:9, 6872:8, 6872:12, 6872:14, 6874:19, 6875:18, 6876:5, 6876:13, 6876:24, 6877:14, 6877:19, 6877:22, 6878:1, 6878:5, 6878:9, 6878:17, 6885:3, 6896:13, 6930:3, 6951:13</p> <p>actuarial [1] - 6936:16</p> <p>acutely [2] - 6903:22, 6904:24</p> <p>adapt [1] - 6861:21</p> <p>adaptable [1] - 6961:1</p> <p>adapted [1] - 6961:2</p> <p>add [7] - 6776:25, 6807:12, 6817:5, 6841:3, 6843:20, 6886:21, 6917:12</p> <p>addition [3] - 6794:6, 6798:6, 6816:10</p> <p>additional [8] - 6840:25, 6841:3, 6924:11, 6949:22, 6951:3, 6958:25, 6959:1, 6966:11</p> <p>address [3] - 6782:17, 6824:8, 6847:6</p> <p>addresses [1] - 6802:4</p> <p>addressing [1] - 6783:6</p> <p>adequate [2] - 6900:17, 6935:8</p> <p>adjourned [1] - 6967:5</p> <p>adjusted [1] - 6897:19</p> <p>adjustment [2] - 6851:12, 6868:8</p> <p>adjustments [2] - 6822:4, 6846:16</p> <p>admission [1] - 6946:2</p> <p>admissions [3] - 6867:14, 6868:14, 6872:19</p>	<p>admitted [9] - 6892:1, 6897:20, 6900:13, 6907:8, 6926:9, 6930:8, 6935:16, 6940:1, 6945:14</p> <p>admittedly [1] - 6925:6</p> <p>adopted [2] - 6875:16, 6907:9</p> <p>adopts [1] - 6806:24</p> <p>adroitly [1] - 6946:19</p> <p>advantage [2] - 6779:25, 6823:10</p> <p>advantages [1] - 6956:14</p> <p>adverse [16] - 6786:6, 6811:14, 6869:9, 6872:9, 6876:1, 6877:11, 6877:19, 6877:22, 6878:1, 6878:9, 6878:18, 6896:13, 6899:18, 6903:7, 6930:3, 6951:13</p> <p>adversely [1] - 6899:23</p> <p>advertised [1] - 6909:25</p> <p>advocates [1] - 6925:7</p> <p>affairs [1] - 6917:21</p> <p>affect [2] - 6878:5, 6905:13</p> <p>affected [2] - 6794:5, 6899:23</p> <p>affecting [1] - 6878:6</p> <p>affects [2] - 6835:10, 6904:17</p> <p>affirmatively [1] - 6944:11</p> <p>afford [1] - 6914:17</p> <p>afforded [1] - 6778:24</p> <p>afield [1] - 6850:1</p> <p>afraid [1] - 6922:18</p> <p>AFTERNOON [1] - 6865:1</p> <p>age [1] - 6790:2</p> <p>agencies [1] - 6836:9</p> <p>agency [3] - 6836:7, 6836:18, 6857:13</p> <p>aggregated [1] - 6926:23</p> <p>aggregation [1] - 6964:15</p> <p>aggressively [3] - 6785:10, 6787:25, 6955:20</p> <p>ago [17] - 6807:8, 6857:12, 6860:11, 6867:3, 6868:10, 6889:21, 6894:11, 6898:6, 6901:12, 6901:23, 6906:9, 6906:14, 6913:2, 6920:11, 6940:5, 6946:7, 6962:21</p> <p>agree [22] - 6822:11, 6869:18, 6881:1, 6882:4, 6882:6, 6887:3, 6888:4, 6888:5, 6890:14, 6892:3, 6899:11, 6906:6, 6907:6, 6912:7, 6913:23, 6923:7, 6939:20, 6962:19, 6962:21, 6963:5</p> <p>agreed [5] - 6853:2, 6854:5, 6872:3, 6891:18, 6936:18</p> <p>agreement [8] - 6845:19, 6846:22, 6847:23, 6848:21, 6851:25, 6852:3, 6852:4, 6963:2</p> <p>agreements [4] - 6853:2, 6868:2, 6872:1, 6903:4</p> <p>agrees [2] - 6876:22, 6930:7</p> <p>ahead [20] - 6780:4, 6797:11, 6802:18, 6809:6, 6809:22, 6823:19, 6834:1, 6834:8, 6841:21, 6849:21, 6891:4, 6891:13, 6898:19, 6903:18, 6917:23, 6925:4, 6949:18, 6955:10, 6956:3, 6956:6</p> <p>aid [2] - 6776:15, 6777:5</p>	<p>airline [20] - 6830:15, 6830:18, 6830:21, 6831:1, 6831:22, 6835:18, 6836:5, 6848:13, 6850:13, 6851:19, 6897:9, 6897:10, 6926:2, 6938:1, 6965:9, 6965:13, 6965:14, 6965:15</p> <p>Airlines [6] - 6780:8, 6782:24, 6837:10, 6837:12, 6846:14, 6927:12</p> <p>airlines [15] - 6830:14, 6831:22, 6831:25, 6834:10, 6836:13, 6836:14, 6841:7, 6848:10, 6848:23, 6851:18, 6851:25, 6852:9, 6853:6, 6855:1</p> <p>airplane [1] - 6848:2</p> <p>airport [7] - 6782:25, 6845:6, 6848:13, 6849:25, 6898:7, 6904:20, 6928:25</p> <p>Airport [1] - 6846:8</p> <p>airports [3] - 6848:6, 6848:7, 6849:11</p> <p>Alaska [4] - 6782:23, 6837:9, 6837:12, 6837:24</p> <p>alive [1] - 6818:12</p> <p>all-or-nothing [2] - 6913:15, 6916:12</p> <p>alleged [2] - 6807:9, 6900:6</p> <p>allocated [1] - 6921:16</p> <p>allotted [1] - 6797:17</p> <p>allow [4] - 6782:3, 6858:22, 6859:1, 6859:15</p> <p>allowed [9] - 6781:17, 6785:6, 6785:8, 6786:19, 6813:5, 6813:10, 6856:18, 6858:16, 6906:9</p> <p>allowing [1] - 6863:20</p> <p>allows [2] - 6806:16, 6814:22</p> <p>almost [13] - 6782:23, 6868:9, 6889:5, 6889:20, 6891:23, 6894:10, 6907:18, 6909:10, 6931:13, 6939:1, 6944:9, 6949:20, 6957:1</p> <p>alone [4] - 6894:2, 6901:25, 6909:7, 6954:10</p> <p>alter [1] - 6816:8</p> <p>alternative [6] - 6811:9, 6894:11, 6918:7, 6918:17, 6929:11, 6947:8</p> <p>alternatives [2] - 6920:20, 6922:6</p> <p>alters [1] - 6837:3</p> <p>amenable [1] - 6815:9</p> <p>Amendment [2] - 6924:19, 6962:6</p> <p>amendment [1] - 6884:7</p> <p>AMERICA [1] - 6772:3</p> <p>America [3] - 6880:11, 6881:12, 6932:8</p> <p>American [218] - 6773:11, 6775:1, 6775:3, 6775:5, 6775:7, 6775:9, 6775:10, 6775:12, 6775:14, 6775:17, 6778:20, 6779:12, 6779:19, 6780:19, 6783:7, 6783:13, 6784:9, 6785:6, 6785:8, 6793:18, 6798:16, 6798:23, 6799:5, 6801:23, 6810:17, 6812:18, 6813:11, 6813:17, 6815:12, 6819:19, 6820:10, 6820:17, 6821:1, 6821:11, 6821:21, 6823:23, 6825:2, 6825:6, 6825:13, 6825:15, 6826:17, 6828:20, 6829:16, 6831:5, 6835:18, 6835:19, 6835:23, 6836:12, 6837:4, 6837:19, 6839:2, 6839:11, 6839:14, 6839:20, 6840:3, 6841:11, 6841:24, 6842:10,</p>
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<p>6842:15, 6842:21, 6842:25, 6843:15, 6843:18, 6843:19, 6843:22, 6844:2, 6844:6, 6844:11, 6844:15, 6844:19, 6844:25, 6845:7, 6845:21, 6846:6, 6846:8, 6846:13, 6846:24, 6847:15, 6848:5, 6848:12, 6849:15, 6849:24, 6850:2, 6850:14, 6850:21, 6850:24, 6851:25, 6852:5, 6852:7, 6852:10, 6852:11, 6852:13, 6852:14, 6852:23, 6853:3, 6853:4, 6853:7, 6854:3, 6854:12, 6854:23, 6855:10, 6856:3, 6856:8, 6856:10, 6856:13, 6856:17, 6858:5, 6858:8, 6858:12, 6859:1, 6859:15, 6859:19, 6859:21, 6861:16, 6862:2, 6862:4, 6864:1, 6865:7, 6866:22, 6867:9, 6867:11, 6867:17, 6867:19, 6867:25, 6872:21, 6878:21, 6879:23, 6881:10, 6881:12, 6881:19, 6883:6, 6883:17, 6883:20, 6884:12, 6884:14, 6885:19, 6889:22, 6890:5, 6890:15, 6890:22, 6892:13, 6892:15, 6897:1, 6897:21, 6901:3, 6901:14, 6902:13, 6902:15, 6902:20, 6903:2, 6903:9, 6904:24, 6906:2, 6906:17, 6907:24, 6908:9, 6910:4, 6910:19, 6911:17, 6911:23, 6911:24, 6913:1, 6914:24, 6916:16, 6916:25, 6917:17, 6919:1, 6921:22, 6921:23, 6922:9, 6922:16, 6923:5, 6923:7, 6924:2, 6925:10, 6925:18, 6925:22, 6926:18, 6927:12, 6927:17, 6929:1, 6932:6, 6932:10, 6933:18, 6934:19, 6935:10, 6935:19, 6936:9, 6936:13, 6938:19, 6942:10, 6942:21, 6942:22, 6944:16, 6945:22, 6946:6, 6946:9, 6946:12, 6950:13, 6954:5, 6954:8, 6954:21, 6955:1, 6955:3, 6955:19, 6955:22, 6956:11, 6956:13, 6958:25, 6959:1, 6959:8, 6959:10, 6959:18, 6960:13, 6961:1, 6962:17</p> <p>AMERICAN [3] - 6772:10, 6772:10, 6772:15</p> <p>Americans [1] - 6827:5</p> <p>Amex [46] - 6781:9, 6781:17, 6782:5, 6782:8, 6783:18, 6784:4, 6785:2, 6785:9, 6785:12, 6788:15, 6790:13, 6790:15, 6791:10, 6793:24, 6794:24, 6795:8, 6795:9, 6795:22, 6796:2, 6796:10, 6797:5, 6797:21, 6798:2, 6798:5, 6800:14, 6800:18, 6800:21, 6801:3, 6801:7, 6814:15, 6814:19, 6814:22, 6814:24, 6815:4, 6815:7, 6816:16, 6818:15, 6821:5, 6821:9, 6822:1, 6931:22, 6932:4, 6933:17, 6936:17, 6937:21</p> <p>AMEX [91] - 6803:19, 6803:25, 6804:1, 6804:17, 6804:23, 6805:5, 6805:9, 6805:17, 6805:18, 6805:19, 6806:10, 6806:16, 6807:5, 6807:8, 6807:14, 6807:18, 6808:11, 6810:15, 6811:3, 6811:11, 6811:22, 6811:23, 6812:1, 6812:11, 6812:13, 6812:15, 6812:16,</p>	<p>6828:8, 6828:13, 6828:18, 6834:13, 6834:16, 6835:3, 6835:6, 6836:6, 6836:9, 6836:11, 6836:12, 6836:17, 6839:7, 6844:18, 6845:18, 6851:7, 6854:5, 6854:7, 6854:20, 6855:7, 6857:10, 6857:12, 6857:15, 6857:16, 6857:17, 6857:20, 6857:24, 6858:3, 6859:17, 6860:9, 6860:12, 6860:14, 6860:16, 6860:20, 6861:6, 6861:8, 6863:18, 6867:8, 6885:22, 6886:3, 6892:18, 6895:6, 6897:4, 6897:14, 6897:24, 6898:12, 6901:19, 6904:19, 6905:2, 6905:9, 6909:9, 6910:5, 6916:13, 6917:3, 6917:7, 6920:3, 6920:14, 6922:3, 6922:13, 6953:14, 6962:23, 6963:20</p> <p>Amex's [25] - 6782:3, 6789:6, 6815:19, 6816:22, 6816:24, 6817:7, 6817:9, 6817:15, 6817:16, 6820:3, 6820:21, 6821:4, 6825:23, 6827:4, 6829:22, 6845:25, 6862:22, 6862:25, 6863:6, 6879:13, 6894:20, 6896:24, 6905:8, 6907:12, 6933:4</p> <p>amount [5] - 6777:11, 6840:17, 6849:20, 6919:17, 6938:12</p> <p>amounts [2] - 6957:14, 6965:6</p> <p>analogous [1] - 6941:19</p> <p>analogy [5] - 6831:7, 6831:20, 6832:18, 6928:22, 6935:17</p> <p>analysis [24] - 6801:5, 6803:18, 6809:2, 6809:15, 6811:13, 6816:8, 6825:14, 6828:6, 6828:9, 6832:19, 6833:16, 6844:4, 6850:8, 6873:15, 6874:15, 6874:16, 6924:19, 6924:24, 6926:18, 6928:20, 6939:5, 6951:16, 6962:11, 6964:25</p> <p>analysts [2] - 6890:4, 6890:10</p> <p>analyze [2] - 6833:1, 6838:20</p> <p>analyzed [1] - 6843:7</p> <p>Andrew [1] - 6774:19</p> <p>ANDREW [1] - 6773:8</p> <p>anecdotal [2] - 6929:20, 6930:12</p> <p>angry [5] - 6845:3, 6845:4, 6937:11, 6939:18, 6939:25</p> <p>announced [2] - 6883:11, 6909:20</p> <p>annoyed [2] - 6844:21, 6844:22</p> <p>annoying [2] - 6857:2, 6857:14</p> <p>annually [1] - 6863:12</p> <p>answer [37] - 6792:21, 6796:18, 6796:22, 6796:24, 6820:19, 6823:15, 6824:17, 6825:23, 6826:11, 6831:1, 6831:20, 6833:18, 6837:20, 6837:21, 6861:7, 6862:3, 6868:19, 6868:20, 6879:19, 6884:3, 6888:20, 6890:13, 6907:25, 6917:9, 6946:5, 6947:6, 6948:3, 6950:20, 6953:6, 6956:7, 6956:10, 6959:14, 6960:24, 6960:25, 6963:13, 6964:6</p> <p>answered [2] - 6838:5, 6953:9</p> <p>answering [3] - 6830:23, 6889:2, 6948:22</p>	<p>ANTI [1] - 6772:15</p> <p>anti [45] - 6781:19, 6783:13, 6783:18, 6785:8, 6786:20, 6790:19, 6791:24, 6792:18, 6792:22, 6793:10, 6793:18, 6793:24, 6795:13, 6811:15, 6811:25, 6812:2, 6812:3, 6815:14, 6815:21, 6815:23, 6816:14, 6820:18, 6821:10, 6838:24, 6857:25, 6861:3, 6862:3, 6862:5, 6862:10, 6862:12, 6862:22, 6864:3, 6870:7, 6874:19, 6875:13, 6882:14, 6882:20, 6885:20, 6896:6, 6911:11, 6911:15, 6912:12, 6952:16, 6954:24, 6957:10</p> <p>anti-competitive [13] - 6811:15, 6812:3, 6838:24, 6870:7, 6874:19, 6875:13, 6882:14, 6882:20, 6896:6, 6911:11, 6911:15, 6912:12, 6954:24</p> <p>anti-steering [32] - 6781:19, 6783:13, 6783:18, 6785:8, 6786:20, 6790:19, 6791:24, 6792:18, 6792:22, 6793:10, 6793:18, 6793:24, 6795:13, 6811:25, 6812:2, 6815:14, 6815:21, 6815:23, 6816:14, 6820:18, 6821:10, 6857:25, 6861:3, 6862:3, 6862:5, 6862:10, 6862:12, 6862:22, 6864:3, 6885:20, 6952:16, 6957:10</p> <p>ANTI-STEERING [1] - 6772:15</p> <p>anticompetitive [17] - 6783:12, 6783:21, 6785:3, 6794:15, 6794:20, 6795:12, 6800:4, 6801:2, 6801:20, 6802:2, 6802:15, 6815:2, 6929:11, 6930:1, 6930:5, 6930:10, 6936:24</p> <p>antisteering [3] - 6838:1, 6958:6, 6959:17</p> <p>ANTITRUST [2] - 6772:15, 6773:2</p> <p>antitrust [65] - 6782:10, 6783:16, 6783:19, 6789:16, 6789:19, 6801:4, 6803:17, 6808:14, 6809:15, 6810:15, 6810:20, 6810:23, 6811:6, 6816:8, 6818:19, 6819:3, 6819:9, 6819:10, 6821:14, 6822:2, 6824:8, 6830:24, 6831:11, 6832:19, 6833:1, 6858:21, 6859:3, 6859:12, 6859:15, 6861:10, 6861:22, 6862:11, 6874:3, 6874:15, 6879:5, 6889:18, 6894:19, 6896:4, 6896:6, 6896:18, 6896:23, 6910:2, 6913:4, 6928:15, 6930:11, 6934:15, 6934:21, 6936:7, 6940:7, 6941:19, 6944:3, 6945:5, 6953:10, 6956:7, 6959:12, 6960:12, 6960:16, 6960:21, 6961:22, 6964:18, 6965:1, 6965:8</p> <p>Antonio [1] - 6965:17</p> <p>anyway [1] - 6811:21</p> <p>app [1] - 6793:12</p> <p>apparent [1] - 6854:13</p> <p>appeals [1] - 6958:8</p> <p>Appeals [1] - 6839:5</p> <p>appear [1] - 6926:13</p> <p>appearances [1] - 6774:6</p> <p>APPEARANCES [1] - 6773:1</p> <p>Apple [2] - 6936:19, 6948:13</p>
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<p>apples [3] - 6850:12, 6850:20</p> <p>applied [2] - 6874:25, 6878:2</p> <p>applies [4] - 6801:14, 6876:6, 6950:19, 6965:20</p> <p>apply [9] - 6817:11, 6870:14, 6871:8, 6874:22, 6875:7, 6875:16, 6878:16, 6884:9, 6899:16</p> <p>applying [3] - 6800:23, 6827:25, 6961:14</p> <p>appreciate [2] - 6864:5, 6949:7</p> <p>approach [13] - 6790:9, 6804:11, 6807:22, 6807:23, 6808:21, 6815:18, 6815:19, 6816:7, 6816:10, 6817:9, 6837:11, 6865:4, 6875:15</p> <p>appropriate [9] - 6790:16, 6825:3, 6828:1, 6831:21, 6859:3, 6859:7, 6947:16, 6947:20, 6966:2</p> <p>appropriately [1] - 6843:12</p> <p>approved [1] - 6938:20</p> <p>architect [1] - 6889:6</p> <p>area [5] - 6828:4, 6828:6, 6835:8, 6905:12, 6951:6</p> <p>argue [5] - 6845:1, 6886:11, 6932:11, 6950:10, 6961:17</p> <p>argued [4] - 6850:17, 6860:1, 6876:22, 6931:20</p> <p>argues [1] - 6875:1</p> <p>arguing [1] - 6932:12</p> <p>argument [31] - 6774:5, 6775:20, 6791:10, 6802:7, 6809:20, 6810:17, 6815:20, 6820:3, 6820:13, 6820:19, 6845:25, 6850:7, 6850:16, 6850:21, 6850:24, 6857:9, 6859:11, 6859:24, 6862:20, 6881:20, 6882:17, 6886:5, 6915:23, 6929:19, 6933:9, 6950:8, 6954:21, 6954:22, 6956:17, 6957:14, 6961:19</p> <p>arguments [4] - 6839:21, 6839:22, 6851:1, 6950:2</p> <p>arithmetic [1] - 6897:4</p> <p>armada [1] - 6926:22</p> <p>arms [3] - 6812:3, 6901:23, 6902:3</p> <p>arose [1] - 6874:7</p> <p>arrangement [5] - 6837:15, 6837:23, 6849:22, 6876:2, 6937:17</p> <p>arrangements [6] - 6833:9, 6833:10, 6848:11, 6857:20, 6873:17, 6875:13</p> <p>articulates [1] - 6825:13</p> <p>artificially [1] - 6923:3</p> <p>aside [3] - 6869:13, 6896:25, 6927:15</p> <p>aspect [1] - 6915:6</p> <p>aspects [3] - 6846:23, 6960:2, 6960:6</p> <p>aspirational [1] - 6900:24</p> <p>assessment [1] - 6852:6</p> <p>asset [2] - 6832:21, 6833:3</p> <p>assets [4] - 6957:8, 6957:11, 6959:8, 6960:20</p> <p>Assistant [3] - 6867:6, 6883:17, 6886:17</p> <p>Assisted [1] - 6772:25</p> <p>associated [1] - 6914:22</p>	<p>Association [1] - 6875:6</p> <p>association [2] - 6890:8, 6900:13</p> <p>associations [1] - 6950:12</p> <p>assume [5] - 6843:21, 6869:20, 6886:7, 6910:21, 6954:3</p> <p>assuming [1] - 6930:1</p> <p>attack [1] - 6946:6</p> <p>attempt [1] - 6907:10</p> <p>attempted [1] - 6945:20</p> <p>attempting [2] - 6907:1, 6955:20</p> <p>attention [1] - 6950:4</p> <p>Attorney [3] - 6867:6, 6883:17, 6886:18</p> <p>attractive [7] - 6815:10, 6834:14, 6843:13, 6860:25, 6959:11, 6960:2, 6960:4</p> <p>Australia [3] - 6888:9, 6888:16, 6892:9</p> <p>authority [6] - 6830:7, 6830:10, 6848:14, 6859:6, 6965:21, 6966:7</p> <p>available [10] - 6778:16, 6801:4, 6845:7, 6857:17, 6865:8, 6877:20, 6908:12, 6920:7, 6920:9, 6920:11</p> <p>Avenue [2] - 6773:12, 6773:16</p> <p>average [2] - 6851:10, 6868:7</p> <p>aviation [2] - 6847:5, 6847:6</p> <p>avoid [2] - 6790:7, 6876:18</p> <p>aware [1] - 6903:22</p>	<p>basket [1] - 6946:6</p> <p>batting [1] - 6937:3</p> <p>bear [1] - 6959:9</p> <p>bearing [1] - 6964:19</p> <p>bearings [1] - 6964:17</p> <p>bears [1] - 6930:15</p> <p>beat [1] - 6786:23</p> <p>become [3] - 6866:23, 6918:9, 6935:17</p> <p>BEFORE [1] - 6772:19</p> <p>began [1] - 6866:6</p> <p>begin [3] - 6866:6, 6896:22, 6955:8</p> <p>beginning [3] - 6825:14, 6838:16, 6939:19</p> <p>behalf [4] - 6836:10, 6862:19, 6864:4, 6884:21</p> <p>behavior [1] - 6904:12</p> <p>behind [3] - 6810:7, 6826:12, 6890:8</p> <p>belabor [1] - 6949:22</p> <p>belong [1] - 6811:19</p> <p>belongs [2] - 6811:20, 6824:19</p> <p>below [1] - 6829:12</p> <p>benefit [29] - 6788:19, 6794:1, 6808:12, 6808:19, 6812:12, 6814:19, 6814:21, 6815:2, 6815:12, 6816:3, 6817:4, 6838:21, 6840:4, 6842:1, 6844:14, 6844:16, 6845:8, 6848:15, 6850:19, 6879:23, 6880:19, 6911:23, 6921:16, 6933:5, 6939:5, 6939:16, 6949:22, 6960:9</p> <p>benefits [25] - 6803:5, 6803:10, 6808:1, 6811:11, 6812:2, 6812:16, 6815:23, 6815:25, 6817:14, 6817:20, 6818:8, 6835:2, 6842:12, 6843:21, 6858:25, 6859:20, 6861:23, 6863:4, 6880:4, 6880:22, 6881:17, 6883:20, 6905:1, 6940:21, 6941:15</p> <p>benefitting [1] - 6941:24</p> <p>BENNET [1] - 6773:6</p> <p>BENNETT [2] - 6774:12, 6777:6</p> <p>Bennett [1] - 6774:13</p> <p>Bernheim [18] - 6806:24, 6825:4, 6841:23, 6842:8, 6842:19, 6843:19, 6844:8, 6851:1, 6851:4, 6852:2, 6853:14, 6853:18, 6861:7, 6894:23, 6895:4, 6915:22, 6924:9, 6924:10</p> <p>Bernheim's [7] - 6843:25, 6851:16, 6853:13, 6908:13, 6913:21, 6919:18, 6924:25</p> <p>Best [1] - 6813:8</p> <p>best [11] - 6786:5, 6797:18, 6809:8, 6812:11, 6862:3, 6867:17, 6891:18, 6902:18, 6902:25, 6906:9, 6945:25</p> <p>better [17] - 6777:23, 6781:25, 6782:15, 6785:23, 6789:14, 6792:19, 6794:17, 6808:20, 6814:24, 6823:14, 6831:19, 6870:8, 6889:13, 6894:4, 6903:13, 6903:15, 6953:14</p> <p>between [19] - 6781:12, 6800:6, 6805:7, 6806:23, 6817:19, 6830:16, 6830:17, 6831:15, 6852:23, 6863:8, 6874:4, 6917:1, 6919:10, 6919:13, 6923:4,</p>
B		
<p>backfired [2] - 6841:18, 6844:21</p> <p>backhanding [1] - 6932:12</p> <p>bad [2] - 6887:25, 6959:15</p> <p>badger [1] - 6957:16</p> <p>baked [1] - 6847:16</p> <p>balance [3] - 6894:9, 6914:15, 6914:18</p> <p>ball [2] - 6964:17, 6964:19</p> <p>bank [6] - 6833:12, 6848:18, 6880:13, 6894:1, 6936:18, 6942:25</p> <p>Bank [3] - 6805:20, 6899:6, 6919:8</p> <p>banker [1] - 6834:13</p> <p>banking [1] - 6833:13</p> <p>banks [10] - 6796:6, 6805:10, 6852:24, 6867:22, 6890:8, 6903:5, 6903:9, 6932:3, 6932:7, 6950:12</p> <p>bar [3] - 6841:4, 6841:5, 6940:25</p> <p>BARBER [2] - 6773:20, 6775:13</p> <p>Barber [1] - 6775:14</p> <p>BARBUR [1] - 6773:14</p> <p>barely [1] - 6945:25</p> <p>bargain [1] - 6849:1</p> <p>bargaining [1] - 6863:7</p> <p>Barrel [1] - 6834:21</p> <p>barriers [1] - 6853:25</p> <p>base [2] - 6885:12, 6956:21</p> <p>based [5] - 6817:16, 6863:4, 6868:24, 6900:1, 6925:22</p> <p>basement [1] - 6908:2</p> <p>basic [2] - 6782:5, 6825:8</p> <p>basis [11] - 6816:19, 6831:15, 6886:19, 6892:7, 6897:2, 6897:19, 6899:9, 6934:10, 6934:16, 6934:25, 6941:7</p>		

<p>6944:18, 6945:4, 6947:4, 6951:9 beyond [8] - 6801:17, 6884:19, 6892:9, 6904:2, 6911:18, 6942:14 bicycles [1] - 6850:21 Bicycles [1] - 6942:17 bid [1] - 6834:15 bidding [1] - 6933:10 bids [1] - 6834:23 Big [1] - 6927:24 big [6] - 6797:5, 6809:25, 6842:24, 6889:11, 6933:16, 6963:23 bigger [3] - 6836:9, 6951:24, 6962:16 biggest [3] - 6868:25, 6902:24, 6903:2 bike [1] - 6942:17 bill [3] - 6915:12, 6915:14, 6926:4 Bill [1] - 6828:20 billion [9] - 6782:19, 6841:2, 6850:9, 6850:10, 6863:12, 6908:14, 6908:25, 6935:3, 6935:4 bills [1] - 6938:1 Biornstad [1] - 6795:19 bit [6] - 6830:7, 6855:7, 6856:9, 6861:22, 6925:2, 6962:6 black [1] - 6853:14 blanche [1] - 6834:3 blank [1] - 6895:2 blast [1] - 6889:16 blasting [1] - 6905:2 blatant [1] - 6945:9 blended [3] - 6921:19, 6922:3, 6923:11 blending [2] - 6921:20, 6921:22 block [8] - 6782:4, 6782:16, 6791:25, 6792:1, 6792:18, 6810:9, 6819:1, 6960:16 blocked [10] - 6782:15, 6784:8, 6785:4, 6785:18, 6791:19, 6792:22, 6793:3, 6793:4, 6795:25, 6838:1 blocking [2] - 6792:23, 6860:13 blue [8] - 6805:15, 6829:11, 6840:16, 6841:4, 6853:17, 6865:22, 6865:24, 6866:1 Blue [1] - 6853:16 Board [1] - 6792:11 board [10] - 6804:22, 6806:18, 6889:8, 6890:3, 6905:4, 6907:23, 6917:17, 6918:16, 6918:22, 6925:9 boards [2] - 6893:25, 6894:1 boIES [1] - 6773:15 bonds [1] - 6908:1 bonus [1] - 6936:5 bonuses [1] - 6936:10 book [3] - 6793:2, 6895:3, 6906:14 bootstrap [1] - 6859:3 born [2] - 6893:17, 6941:12 borrowing [1] - 6880:13 Boston [1] - 6919:8 bottom [3] - 6816:25, 6853:15, 6958:4 Bouchard [1] - 6827:10 boundaries [1] - 6829:17 box [3] - 6805:15, 6829:11, 6907:23 bracket [1] - 6877:13</p>	<p>branch [1] - 6961:22 brand [10] - 6857:16, 6871:3, 6873:22, 6907:3, 6922:14, 6923:7, 6923:8, 6923:10, 6923:12, 6956:22 break [9] - 6777:15, 6822:21, 6822:23, 6823:11, 6859:9, 6864:8, 6901:17, 6949:10 breaking [2] - 6777:24, 6901:13 Brenner [1] - 6775:7 BRENNER [2] - 6773:17, 6775:6 Bridge [1] - 6942:18 brief [10] - 6781:10, 6820:21, 6845:2, 6850:9, 6862:20, 6868:15, 6900:12, 6949:5, 6949:17, 6949:19 briefing [1] - 6779:3 briefly [5] - 6794:19, 6796:8, 6838:14, 6838:18, 6964:9 BRIGHT [2] - 6773:20, 6775:16 bright [1] - 6775:15 Bright [1] - 6775:17 bring [3] - 6860:16, 6860:25, 6959:8 brings [3] - 6819:23, 6883:2, 6960:20 broad [2] - 6782:8, 6964:22 broader [1] - 6827:22 broadly [1] - 6818:1 broken [17] - 6780:8, 6780:11, 6780:13, 6780:24, 6782:18, 6783:3, 6789:15, 6789:25, 6800:6, 6866:7, 6866:9, 6866:18, 6897:22, 6898:23, 6903:19 Brooklyn [2] - 6772:9, 6772:23 brought [9] - 6840:7, 6841:1, 6867:10, 6867:12, 6867:25, 6868:13, 6884:18, 6884:20, 6942:13 Brown [2] - 6824:3, 6859:25 bucks [6] - 6813:13, 6813:18, 6813:25, 6814:1, 6927:20, 6935:3 bump [1] - 6842:24 bump-up [1] - 6842:24 bunch [5] - 6798:16, 6884:3, 6890:8, 6926:23, 6932:20 burden [12] - 6801:17, 6804:8, 6811:16, 6811:20, 6811:22, 6815:1, 6815:5, 6815:16, 6815:20, 6815:24, 6816:13, 6952:20 Burger [3] - 6927:25, 6928:6, 6928:8 business [98] - 6780:20, 6781:13, 6781:20, 6785:13, 6785:14, 6785:17, 6785:21, 6785:22, 6786:1, 6786:16, 6787:18, 6787:19, 6788:25, 6789:1, 6789:6, 6789:8, 6791:22, 6793:9, 6794:7, 6795:6, 6799:19, 6800:7, 6800:17, 6802:3, 6804:18, 6804:21, 6812:1, 6812:12, 6816:15, 6819:14, 6820:15, 6820:18, 6821:2, 6821:5, 6821:9, 6821:12, 6822:1, 6822:3, 6822:8, 6822:19, 6827:9, 6830:6, 6832:2, 6832:14, 6836:3, 6836:4, 6837:18, 6837:19, 6837:25, 6851:7, 6851:9, 6859:11, 6860:8, 6860:10, 6860:17, 6860:21, 6860:22, 6860:23, 6860:24, 6861:2, 6861:13, 6862:1,</p>	<p>6862:6, 6880:24, 6889:23, 6901:4, 6902:21, 6902:22, 6905:5, 6905:16, 6906:8, 6908:7, 6908:11, 6909:2, 6920:23, 6922:10, 6923:22, 6928:4, 6933:11, 6935:14, 6935:20, 6935:21, 6937:5, 6942:23, 6944:21, 6945:3, 6945:10, 6951:9, 6952:9, 6954:6, 6958:14, 6959:20, 6960:7, 6960:14, 6960:22 Business [2] - 6886:7, 6886:8 businesses [2] - 6784:14, 6863:19 busy [1] - 6858:6 BUTLER [1] - 6772:22 Buy [1] - 6813:8 buy [9] - 6813:9, 6843:15, 6846:14, 6921:8, 6927:12, 6927:24, 6928:25, 6942:24 buyers [2] - 6831:23, 6939:10 buying [2] - 6880:21, 6881:8 BY [8] - 6773:4, 6773:13, 6773:17, 6778:10, 6823:8, 6968:7, 6968:9, 6968:11 bypass [1] - 6955:19</p>
C		
<p>cab [3] - 6927:14, 6927:15 Cadman [1] - 6772:23 calculate [1] - 6828:24 calculates [1] - 6854:20 calculation [2] - 6844:1, 6853:13 calculations [2] - 6926:20, 6927:1 calculus [2] - 6837:4, 6916:8 Califano [1] - 6775:12 CALIFANO [2] - 6773:19, 6775:11 California [1] - 6875:5 call-to-arms [1] - 6901:23 campaign [18] - 6795:13, 6795:15, 6795:17, 6798:18, 6868:3, 6894:11, 6901:12, 6903:21, 6904:2, 6905:10, 6905:22, 6906:15, 6911:18, 6911:21, 6911:22, 6911:25, 6945:18 campaigns [4] - 6794:22, 6800:10, 6854:24, 6911:17 Canada [5] - 6888:6, 6888:8, 6888:16, 6892:9 cancel [2] - 6849:14, 6916:16 cancellation [1] - 6936:14 cancelled [1] - 6909:22 cancelling [1] - 6909:21 Cannes [2] - 6889:8, 6893:23 cannot [9] - 6781:3, 6785:13, 6827:16, 6858:24, 6873:10, 6892:1, 6899:8, 6930:9 Capital [4] - 6801:14, 6900:10, 6900:12, 6900:16 capitalized [1] - 6877:13 captives [1] - 6942:4 capturing [1] - 6939:13 car [1] - 6829:10 card [148] - 6778:20, 6780:12, 6781:6,</p>		

<p>6782:1, 6782:20, 6782:21, 6782:22, 6782:24, 6783:1, 6783:3, 6785:12, 6786:2, 6786:18, 6788:12, 6789:5, 6790:4, 6790:24, 6792:7, 6793:14, 6793:17, 6795:3, 6798:6, 6798:7, 6798:21, 6799:13, 6799:21, 6800:19, 6804:17, 6804:23, 6804:25, 6805:13, 6807:9, 6807:24, 6808:15, 6813:10, 6813:11, 6813:13, 6814:4, 6814:11, 6816:10, 6818:1, 6820:6, 6824:15, 6824:20, 6826:6, 6827:13, 6827:16, 6827:17, 6827:22, 6832:1, 6832:15, 6833:9, 6833:13, 6833:15, 6834:21, 6834:22, 6834:24, 6835:7, 6835:13, 6835:14, 6836:16, 6836:20, 6845:7, 6846:13, 6846:15, 6852:11, 6853:3, 6853:4, 6854:19, 6856:8, 6856:13, 6863:5, 6863:8, 6863:9, 6863:11, 6877:18, 6877:20, 6881:10, 6881:12, 6883:20, 6889:22, 6892:2, 6902:10, 6905:5, 6905:13, 6906:1, 6907:2, 6909:12, 6909:13, 6911:8, 6914:11, 6914:23, 6915:2, 6915:5, 6915:11, 6915:14, 6918:4, 6918:8, 6918:25, 6919:18, 6920:2, 6920:3, 6920:5, 6920:6, 6920:14, 6920:15, 6920:16, 6921:7, 6921:10, 6922:13, 6922:15, 6922:18, 6923:7, 6923:8, 6923:10, 6927:17, 6929:1, 6929:4, 6930:25, 6931:2, 6931:10, 6933:10, 6933:16, 6933:17, 6936:18, 6939:9, 6944:13, 6944:18, 6944:19, 6950:12, 6950:15, 6953:15, 6955:3, 6957:7, 6958:10, 6960:1, 6963:3</p> <p>cardholder [13] - 6804:25, 6814:18, 6817:19, 6817:20, 6817:25, 6818:9, 6842:11, 6842:13, 6843:20, 6845:8, 6859:20, 6861:15, 6905:25</p> <p>Cardholders [1] - 6858:8</p> <p>cardholders [55] - 6781:18, 6803:5, 6804:9, 6805:8, 6805:10, 6806:6, 6806:12, 6807:14, 6808:12, 6808:18, 6808:20, 6810:12, 6811:2, 6812:11, 6812:16, 6812:17, 6813:4, 6813:5, 6815:8, 6815:12, 6815:15, 6816:3, 6816:4, 6816:18, 6816:20, 6817:1, 6817:4, 6817:14, 6819:14, 6825:17, 6825:24, 6825:25, 6842:17, 6843:14, 6843:21, 6843:23, 6844:14, 6844:15, 6844:16, 6846:6, 6849:10, 6856:12, 6858:5, 6861:1, 6861:9, 6861:18, 6861:19, 6891:23, 6891:25, 6956:21, 6958:8, 6958:15, 6960:4</p> <p>Cardmembers [2] - 6863:18, 6880:23</p> <p>cards [80] - 6788:4, 6788:5, 6788:6, 6788:8, 6788:22, 6792:8, 6799:16, 6805:9, 6805:10, 6806:7, 6807:3, 6807:13, 6812:8, 6812:9, 6812:10, 6812:19, 6825:12, 6826:6, 6826:10, 6826:13, 6826:14, 6826:15, 6826:16, 6827:3, 6827:6, 6827:7, 6827:9, 6827:13, 6827:16, 6831:4, 6832:10,</p>	<p>6834:10, 6834:16, 6834:25, 6835:4, 6835:6, 6835:11, 6835:19, 6835:20, 6837:7, 6852:5, 6852:14, 6857:16, 6857:19, 6863:17, 6867:20, 6880:14, 6880:24, 6880:25, 6891:20, 6891:24, 6903:10, 6903:11, 6914:4, 6914:5, 6914:15, 6914:24, 6915:3, 6916:14, 6917:5, 6917:22, 6920:13, 6920:18, 6928:5, 6928:7, 6930:20, 6932:9, 6936:9, 6950:4, 6955:1, 6961:25, 6962:1, 6963:20, 6964:1, 6964:7, 6964:8</p> <p>care [3] - 6909:9, 6930:11, 6955:24</p> <p>carefully [1] - 6839:9</p> <p>carries [2] - 6910:12, 6944:18</p> <p>carry [8] - 6880:13, 6881:11, 6914:15, 6940:24, 6941:3, 6941:5, 6943:3</p> <p>carrying [3] - 6880:24, 6880:25, 6881:14</p> <p>cars [2] - 6897:8</p> <p>carte [1] - 6834:3</p> <p>CARTER [2] - 6773:7, 6774:15</p> <p>Carter [1] - 6774:15</p> <p>case [150] - 6778:15, 6778:18, 6779:6, 6779:13, 6779:20, 6782:4, 6783:7, 6783:17, 6784:1, 6790:13, 6794:12, 6794:18, 6801:9, 6801:15, 6801:18, 6801:20, 6801:22, 6803:6, 6803:7, 6803:24, 6806:13, 6808:3, 6808:4, 6808:6, 6809:13, 6811:1, 6816:6, 6818:20, 6830:11, 6831:8, 6832:4, 6840:7, 6849:24, 6853:7, 6859:6, 6859:24, 6863:21, 6866:10, 6866:13, 6866:23, 6867:5, 6867:15, 6868:23, 6869:5, 6869:15, 6870:3, 6870:4, 6870:5, 6870:9, 6870:15, 6871:5, 6871:6, 6871:12, 6871:25, 6873:9, 6873:12, 6874:9, 6874:11, 6874:23, 6874:25, 6875:3, 6875:4, 6875:6, 6875:16, 6875:20, 6875:21, 6876:3, 6876:4, 6876:16, 6876:23, 6877:7, 6877:8, 6877:14, 6879:17, 6880:1, 6882:1, 6882:5, 6882:10, 6882:15, 6882:22, 6883:17, 6885:22, 6886:8, 6886:22, 6887:11, 6887:20, 6887:24, 6890:11, 6896:9, 6898:6, 6899:6, 6899:7, 6899:11, 6899:12, 6899:15, 6899:20, 6899:25, 6900:1, 6900:3, 6900:4, 6900:8, 6900:10, 6900:23, 6901:25, 6902:1, 6903:23, 6906:24, 6912:20, 6912:21, 6913:3, 6913:5, 6917:2, 6920:9, 6924:8, 6924:9, 6929:15, 6930:21, 6931:19, 6931:20, 6931:23, 6932:2, 6932:20, 6932:25, 6933:1, 6934:15, 6940:9, 6940:16, 6940:19, 6941:20, 6942:2, 6942:3, 6942:5, 6944:1, 6944:15, 6946:9, 6946:10, 6946:13, 6948:6, 6948:13, 6951:5, 6952:9, 6952:14, 6955:22, 6961:1, 6965:21</p> <p>case-by-case [1] - 6899:25</p> <p>cases [27] - 6779:1, 6801:6, 6801:10,</p>	<p>6801:11, 6801:13, 6866:10, 6870:11, 6871:19, 6873:15, 6873:23, 6874:5, 6874:6, 6874:12, 6874:17, 6875:17, 6875:19, 6877:5, 6899:6, 6911:14, 6912:10, 6912:15, 6912:17, 6928:15, 6932:21, 6934:13, 6945:7, 6964:18</p> <p>cash [8] - 6812:10, 6863:16, 6880:7, 6880:12, 6904:6, 6904:9, 6915:8, 6941:7</p> <p>catch [2] - 6898:19, 6898:20</p> <p>categories [3] - 6782:8, 6829:24, 6830:1</p> <p>category [5] - 6782:12, 6782:14, 6794:23, 6821:21, 6839:12</p> <p>caught [1] - 6946:22</p> <p>causation [1] - 6850:16</p> <p>caused [1] - 6845:5</p> <p>causes [1] - 6857:21</p> <p>causing [2] - 6857:16, 6857:21</p> <p>Centurion [1] - 6848:8</p> <p>CEO [3] - 6866:23, 6890:5, 6890:9</p> <p>certain [4] - 6779:4, 6937:21, 6961:12, 6961:25</p> <p>certainly [10] - 6778:23, 6780:3, 6789:7, 6789:10, 6799:2, 6849:4, 6876:22, 6941:19, 6955:20, 6963:23</p> <p>cetera [2] - 6867:22, 6880:14</p> <p>CFO [1] - 6816:22</p> <p>chain [1] - 6836:5</p> <p>chair [1] - 6937:7</p> <p>chairman [1] - 6890:3</p> <p>challenge [3] - 6799:11, 6822:2, 6882:10</p> <p>challenges [2] - 6958:23, 6961:2</p> <p>Chambers [1] - 6893:9</p> <p>chance [5] - 6842:23, 6860:16, 6860:20, 6860:21, 6952:19</p> <p>change [10] - 6788:3, 6846:12, 6850:3, 6869:8, 6871:1, 6882:18, 6884:15, 6924:22, 6957:9, 6962:7</p> <p>changed [4] - 6868:13, 6868:16, 6872:25, 6939:15</p> <p>changes [4] - 6822:5, 6851:14, 6961:25, 6962:1</p> <p>changing [1] - 6848:9</p> <p>channel [1] - 6859:18</p> <p>channelled [1] - 6788:18</p> <p>character [1] - 6796:23</p> <p>characteristics [1] - 6803:12</p> <p>characterize [2] - 6782:9, 6913:9</p> <p>characterized [1] - 6821:2</p> <p>charge [31] - 6790:4, 6798:6, 6832:15, 6850:9, 6850:13, 6862:24, 6863:5, 6863:8, 6863:9, 6863:11, 6873:21, 6892:14, 6897:13, 6913:1, 6914:4, 6914:22, 6914:23, 6915:11, 6918:6, 6918:8, 6918:17, 6919:23, 6920:1, 6921:15, 6922:9, 6922:19, 6923:8, 6926:8, 6931:12, 6960:6</p> <p>charged [1] - 6914:9</p> <p>charges [6] - 6839:11, 6897:11,</p>
---	--	---

<p>6921:12, 6921:14, 6921:20, 6925:18 charging [2] - 6937:5, 6939:23 chart [11] - 6804:24, 6805:2, 6851:21, 6853:10, 6894:22, 6894:23, 6895:3, 6919:16, 6931:8, 6940:17, 6952:15 charts [2] - 6853:9, 6921:24 Chase [28] - 6845:17, 6845:19, 6845:23, 6845:24, 6846:6, 6846:13, 6846:22, 6846:25, 6847:13, 6848:17, 6848:18, 6848:19, 6848:20, 6848:25, 6849:2, 6849:5, 6849:7, 6849:16, 6849:17, 6849:21, 6898:12, 6937:13, 6937:17, 6955:12, 6955:16, 6956:11, 6958:24, 6959:2 Chase's [1] - 6955:18 cheap [3] - 6789:9, 6789:13, 6960:2 cheaper [13] - 6780:20, 6780:23, 6788:13, 6788:14, 6789:11, 6792:20, 6794:24, 6795:3, 6795:6, 6851:9, 6959:21, 6959:23, 6959:25 cheapest [1] - 6862:24 check [6] - 6880:7, 6880:12, 6927:16, 6930:6, 6930:11, 6941:7 checking [1] - 6915:7 checkout [2] - 6857:15, 6858:1 checks [1] - 6812:10 Chenault [20] - 6798:5, 6798:15, 6799:9, 6821:24, 6857:18, 6867:4, 6888:25, 6889:3, 6892:6, 6894:5, 6897:17, 6898:19, 6901:22, 6903:14, 6906:10, 6933:7, 6940:13, 6945:17, 6945:24, 6954:3 Chenault's [4] - 6798:24, 6867:16, 6889:9, 6906:6 CHESLER [51] - 6773:13, 6774:25, 6776:13, 6776:22, 6777:7, 6777:10, 6777:21, 6778:1, 6840:12, 6865:19, 6865:25, 6866:3, 6866:5, 6875:10, 6885:23, 6886:14, 6886:19, 6886:24, 6891:1, 6891:3, 6891:5, 6891:10, 6891:14, 6896:1, 6899:1, 6909:17, 6914:25, 6915:4, 6915:10, 6915:16, 6923:2, 6925:5, 6938:16, 6938:22, 6938:25, 6944:1, 6946:17, 6946:21, 6946:23, 6947:6, 6947:14, 6947:24, 6948:2, 6948:15, 6948:18, 6948:21, 6949:1, 6955:8, 6966:20, 6967:2, 6968:9 Chesler [6] - 6775:1, 6797:15, 6822:10, 6865:18, 6966:1, 6967:1 chest [1] - 6929:2 Chicago [5] - 6830:17, 6830:20, 6927:12, 6928:23, 6928:24 chief [1] - 6845:15 child [1] - 6931:23 chips [4] - 6876:10, 6883:1, 6907:22, 6907:23 chocolate [1] - 6928:25 choice [13] - 6813:11, 6813:14, 6813:15, 6813:18, 6813:19, 6813:22, 6814:14, 6814:16, 6814:25, 6853:18,</p>	<p>6933:4, 6938:7, 6941:23 ChoicePay [1] - 6793:22 choke [2] - 6889:14, 6904:25 choose [5] - 6810:13, 6813:16, 6833:12, 6835:1, 6836:4 choosing [1] - 6793:17 chop [1] - 6928:9 chopping [1] - 6928:10 chosen [1] - 6881:14 Christopher [1] - 6780:8 chunk [2] - 6826:15, 6963:23 circle [3] - 6889:9, 6889:10, 6935:13 Circuit [19] - 6801:5, 6869:10, 6870:4, 6870:10, 6870:16, 6871:19, 6873:13, 6875:19, 6875:21, 6882:22, 6899:20, 6899:22, 6900:11, 6912:15, 6932:16, 6932:21, 6941:11, 6948:9, 6948:10 circuit [1] - 6912:22 circumstances [1] - 6904:12 citation [1] - 6882:23 cite [14] - 6801:11, 6801:12, 6830:9, 6859:6, 6874:5, 6877:12, 6899:6, 6899:19, 6912:17, 6930:24, 6942:18, 6944:2, 6945:7, 6948:5 cited [9] - 6799:1, 6803:7, 6827:24, 6830:8, 6859:25, 6911:6, 6913:4, 6924:9, 6940:9 cites [2] - 6860:14, 6932:20 citing [1] - 6932:10 city [8] - 6830:16, 6831:1, 6831:8, 6837:11, 6897:11, 6928:20, 6928:23, 6965:9 City [2] - 6858:4, 6912:16 civil [1] - 6774:5 claim [20] - 6820:23, 6821:5, 6821:8, 6821:12, 6841:18, 6841:24, 6842:12, 6844:8, 6845:12, 6850:2, 6850:25, 6856:9, 6856:16, 6858:10, 6876:8, 6876:15, 6900:22, 6956:19 claimed [1] - 6807:11 claims [4] - 6801:3, 6841:22, 6841:23, 6842:7 clarify [1] - 6796:25 classic [3] - 6795:5, 6795:6, 6912:1 clause [1] - 6866:1 clear [16] - 6781:5, 6781:9, 6796:24, 6797:2, 6820:24, 6830:3, 6839:3, 6849:18, 6893:3, 6912:21, 6925:18, 6927:9, 6934:14, 6952:2, 6958:20 clearest [1] - 6952:14 clearly [4] - 6780:19, 6809:2, 6871:9, 6964:22 client [1] - 6898:10 cliff [1] - 6957:17 clock [3] - 6775:20, 6775:21, 6775:22 closed [4] - 6787:4, 6793:25, 6820:1, 6908:10 closely [1] - 6798:20 closest [1] - 6882:15 closing [3] - 6777:12, 6865:17, 6869:23 club [1] - 6893:21</p>	<p>clubhouse [1] - 6893:21 co [5] - 6857:16, 6923:7, 6923:8, 6923:10, 6923:12 co-brand [5] - 6857:16, 6923:7, 6923:8, 6923:10, 6923:12 Cobrand [24] - 6834:10, 6834:14, 6845:17, 6845:19, 6845:23, 6846:12, 6846:15, 6846:22, 6846:23, 6847:23, 6851:25, 6852:3, 6852:16, 6852:17, 6852:21, 6852:22, 6853:1, 6853:4, 6922:7, 6922:8, 6922:11, 6922:12, 6922:18, 6963:2 cognizable [1] - 6819:9 cold [1] - 6820:25 colleagues [3] - 6793:1, 6865:6, 6945:17 collected [1] - 6807:10 colorful [1] - 6879:24 combined [1] - 6931:15 combines [1] - 6807:1 coming [6] - 6808:5, 6844:2, 6875:9, 6917:18, 6918:5, 6918:18 comment [5] - 6779:7, 6821:24, 6885:18, 6949:22, 6962:2 comments [3] - 6777:14, 6868:15, 6869:1 Commercial [1] - 6932:19 commercial [1] - 6927:5 Commission [1] - 6875:6 committee [1] - 6908:10 common [4] - 6933:9, 6964:13, 6965:1, 6966:9 commonly [2] - 6821:13, 6932:6 companies [10] - 6786:21, 6796:7, 6800:8, 6858:20, 6858:21, 6902:21, 6928:15, 6933:10, 6952:1, 6960:24 company [24] - 6784:6, 6784:21, 6793:16, 6832:23, 6833:2, 6833:4, 6833:11, 6867:20, 6889:5, 6889:22, 6890:1, 6890:5, 6890:9, 6890:11, 6894:6, 6915:17, 6918:10, 6930:8, 6934:20, 6936:6, 6958:13, 6960:19 COMPANY [2] - 6772:10, 6772:11 Company [1] - 6773:12 company's [1] - 6917:18 comparable [2] - 6919:12, 6931:19 compare [4] - 6806:16, 6829:10, 6897:20, 6932:5 compared [9] - 6794:25, 6799:25, 6806:17, 6828:14, 6855:8, 6867:21, 6925:16, 6932:9, 6955:16 compares [2] - 6850:9, 6850:10 comparing [3] - 6850:8, 6850:20 comparison [4] - 6831:8, 6831:21, 6850:12, 6932:4 comparisons [1] - 6850:17 compartmentalizing [1] - 6826:18 compelling [2] - 6936:23, 6936:25 compensated [1] - 6795:21 compensation [1] - 6836:19 compete [31] - 6780:21, 6781:17,</p>
---	--	---

<p>6784:16, 6786:7, 6796:14, 6799:24, 6800:1, 6810:17, 6811:4, 6818:16, 6830:21, 6832:21, 6859:2, 6860:3, 6860:5, 6861:11, 6861:13, 6861:25, 6886:3, 6892:23, 6893:4, 6893:13, 6893:17, 6897:8, 6897:10, 6905:16, 6921:4, 6931:14, 6950:12, 6955:23, 6960:1</p> <p>competed [1] - 6834:13</p> <p>competing [12] - 6784:14, 6790:10, 6799:17, 6830:12, 6831:15, 6832:2, 6832:23, 6833:5, 6833:7, 6887:16, 6893:14, 6959:3</p> <p>competition [183] - 6780:12, 6781:6, 6782:1, 6782:3, 6782:15, 6782:16, 6783:17, 6783:19, 6783:22, 6784:1, 6784:12, 6785:15, 6785:17, 6786:6, 6787:9, 6787:11, 6787:16, 6787:20, 6787:21, 6788:18, 6788:23, 6789:4, 6789:20, 6789:25, 6790:3, 6791:20, 6792:9, 6792:23, 6792:24, 6795:5, 6795:6, 6795:7, 6795:22, 6795:24, 6795:25, 6797:24, 6799:17, 6800:9, 6801:19, 6803:4, 6805:9, 6806:1, 6806:11, 6806:12, 6806:13, 6806:14, 6807:13, 6807:16, 6808:1, 6808:9, 6808:14, 6808:18, 6808:20, 6808:23, 6808:24, 6810:9, 6810:10, 6810:11, 6810:14, 6810:25, 6811:7, 6811:25, 6814:23, 6815:12, 6815:21, 6816:15, 6819:1, 6819:8, 6819:22, 6821:13, 6824:4, 6824:5, 6828:4, 6828:7, 6830:16, 6830:17, 6830:25, 6831:24, 6832:7, 6832:24, 6833:1, 6834:9, 6834:11, 6834:17, 6834:19, 6835:1, 6835:2, 6835:9, 6835:12, 6835:21, 6837:17, 6849:12, 6852:22, 6852:23, 6858:20, 6858:25, 6859:5, 6859:7, 6859:13, 6859:16, 6859:18, 6859:19, 6859:20, 6859:21, 6859:22, 6860:7, 6860:9, 6860:13, 6861:14, 6862:11, 6862:23, 6863:8, 6863:22, 6867:12, 6869:9, 6872:9, 6873:4, 6873:22, 6877:11, 6877:18, 6877:24, 6878:9, 6878:18, 6886:2, 6887:14, 6887:18, 6887:24, 6889:4, 6889:12, 6892:12, 6892:13, 6892:25, 6897:22, 6897:23, 6898:9, 6899:8, 6899:9, 6902:7, 6902:14, 6906:19, 6913:12, 6913:19, 6913:25, 6914:7, 6916:10, 6917:13, 6918:19, 6918:20, 6924:15, 6945:8, 6946:10, 6950:2, 6950:3, 6950:4, 6950:15, 6950:16, 6950:19, 6950:21, 6950:24, 6950:25, 6951:4, 6951:14, 6952:5, 6952:8, 6952:13, 6953:12, 6953:16, 6953:23, 6953:25, 6954:5, 6954:6, 6954:11, 6954:17, 6956:8, 6956:14, 6958:5, 6958:7, 6959:16, 6960:15, 6960:16, 6961:3</p> <p>competitions [1] - 6807:4</p> <p>competitive [69] - 6780:13, 6783:24, 6784:22, 6785:22, 6787:4, 6787:8,</p>	<p>6789:2, 6789:19, 6790:21, 6790:22, 6792:25, 6795:10, 6798:10, 6799:11, 6800:5, 6801:3, 6801:8, 6802:21, 6811:11, 6811:15, 6811:16, 6811:18, 6812:3, 6815:2, 6817:24, 6819:17, 6832:8, 6832:10, 6838:24, 6858:15, 6859:4, 6860:4, 6863:20, 6868:18, 6869:2, 6869:3, 6870:7, 6874:19, 6875:13, 6877:11, 6880:4, 6882:14, 6882:20, 6883:10, 6883:13, 6896:6, 6896:23, 6898:23, 6899:2, 6899:14, 6902:15, 6903:20, 6911:11, 6911:13, 6911:15, 6912:12, 6920:19, 6923:24, 6924:24, 6934:8, 6934:9, 6951:8, 6952:10, 6954:9, 6954:24, 6957:7, 6958:12, 6958:23, 6959:8</p> <p>competitive-effect [1] - 6899:2</p> <p>competitor [12] - 6781:4, 6784:7, 6791:25, 6810:16, 6860:21, 6861:11, 6867:23, 6918:14, 6923:19, 6930:23, 6946:7, 6963:25</p> <p>competitors [10] - 6780:17, 6780:24, 6800:13, 6831:18, 6831:21, 6859:13, 6873:23, 6903:16, 6918:21, 6956:8</p> <p>complaints [3] - 6909:21, 6910:3, 6910:7</p> <p>completed [3] - 6879:12, 6879:14, 6886:12</p> <p>completely [1] - 6939:20</p> <p>complicated [2] - 6808:22, 6817:23</p> <p>components [2] - 6879:9, 6879:15</p> <p>Computer [1] - 6772:25</p> <p>Computer-Assisted [1] - 6772:25</p> <p>conceded [3] - 6869:5, 6905:18, 6925:21</p> <p>concedes [3] - 6785:2, 6900:12, 6924:8</p> <p>concentrated [1] - 6947:22</p> <p>concentrating [1] - 6947:23</p> <p>concept [2] - 6826:17, 6828:22</p> <p>concern [2] - 6821:25, 6863:22</p> <p>concerning [2] - 6863:1, 6876:1</p> <p>concerns [1] - 6803:24</p> <p>concession [4] - 6925:14, 6936:21</p> <p>concessions [2] - 6800:14, 6923:8</p> <p>conclude [1] - 6875:12</p> <p>concluded [2] - 6828:6, 6838:25</p> <p>concludes [1] - 6801:21</p> <p>conclusion [9] - 6821:25, 6828:25, 6844:3, 6844:16, 6863:25, 6877:9, 6878:4, 6944:1, 6944:4</p> <p>conclusions [4] - 6872:12, 6882:3, 6882:9, 6966:8</p> <p>concrete [2] - 6801:18, 6814:7</p> <p>condemned [2] - 6873:16, 6951:20</p> <p>conditions [4] - 6791:17, 6835:12, 6876:13, 6964:25</p> <p>conduct [5] - 6874:4, 6888:7, 6907:11, 6930:10, 6951:18</p> <p>conference [3] - 6883:11, 6883:15, 6929:18</p> <p>conferring [1] - 6880:3</p>	<p>confidence [1] - 6887:9</p> <p>confidential [3] - 6895:2, 6921:25, 6923:18</p> <p>confidentiality [1] - 6777:3</p> <p>confirmed [6] - 6785:7, 6785:9, 6785:20, 6801:2, 6801:5, 6936:17</p> <p>conflict [1] - 6916:9</p> <p>confront [1] - 6926:25</p> <p>confronted [1] - 6876:12</p> <p>confronting [1] - 6872:17</p> <p>confuse [1] - 6916:10</p> <p>confusion [1] - 6876:18</p> <p>Congress [4] - 6810:24, 6961:16, 6961:17, 6961:24</p> <p>Congressional [1] - 6961:11</p> <p>conjures [2] - 6883:8, 6885:15</p> <p>CONNECTICUT [1] - 6772:4</p> <p>connection [5] - 6781:12, 6802:21, 6804:2, 6951:8, 6952:7</p> <p>CONRATH [109] - 6773:4, 6774:7, 6776:1, 6776:8, 6776:16, 6776:19, 6776:25, 6778:6, 6778:8, 6778:10, 6778:11, 6778:23, 6779:2, 6779:10, 6779:15, 6780:2, 6780:5, 6788:10, 6789:7, 6790:8, 6790:16, 6791:11, 6796:16, 6796:20, 6796:22, 6796:25, 6797:10, 6797:12, 6797:16, 6797:20, 6802:7, 6802:10, 6802:12, 6802:19, 6803:1, 6808:7, 6809:4, 6809:8, 6809:10, 6809:12, 6809:17, 6809:21, 6809:23, 6813:2, 6813:24, 6814:2, 6814:5, 6814:7, 6814:10, 6814:14, 6816:3, 6816:5, 6818:4, 6818:14, 6818:19, 6818:22, 6818:25, 6822:13, 6822:17, 6822:22, 6823:8, 6823:9, 6823:20, 6827:1, 6831:19, 6833:17, 6833:20, 6833:24, 6834:7, 6834:9, 6839:24, 6840:2, 6840:9, 6840:14, 6841:16, 6841:22, 6847:1, 6847:6, 6847:24, 6848:4, 6856:1, 6865:4, 6865:11, 6865:13, 6949:5, 6949:7, 6949:11, 6949:17, 6949:19, 6949:24, 6953:1, 6953:3, 6954:18, 6954:20, 6955:11, 6955:17, 6956:1, 6956:4, 6956:7, 6957:1, 6958:1, 6961:7, 6961:9, 6961:16, 6961:24, 6962:4, 6966:23, 6968:7, 6968:11</p> <p>Conrath [31] - 6774:8, 6778:5, 6822:20, 6866:6, 6868:14, 6871:2, 6871:4, 6871:13, 6872:18, 6878:21, 6879:5, 6879:24, 6881:24, 6889:1, 6889:23, 6894:22, 6896:13, 6907:22, 6912:6, 6913:21, 6916:21, 6918:23, 6924:9, 6931:25, 6937:12, 6937:14, 6938:3, 6938:12, 6940:16, 6949:4, 6949:16</p> <p>Conrath's [1] - 6879:1</p> <p>consequence [1] - 6860:5</p> <p>conservative [2] - 6790:9, 6917:21</p> <p>consider [5] - 6794:11, 6803:15, 6807:20, 6811:10, 6820:6</p> <p>consideration [1] - 6815:13</p>
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<p>considered [5] - 6795:9, 6803:13, 6811:19, 6838:12, 6922:6</p> <p>considering [6] - 6803:16, 6811:11, 6815:16, 6865:21, 6906:19, 6961:22</p> <p>consistent [4] - 6816:23, 6893:12, 6923:14, 6940:8</p> <p>consistently [1] - 6870:16</p> <p>consortium [1] - 6792:12</p> <p>constitute [1] - 6896:17</p> <p>constraining [1] - 6924:23</p> <p>construct [1] - 6947:7</p> <p>constructed [1] - 6923:3</p> <p>consumer [31] - 6793:17, 6818:11, 6825:12, 6868:9, 6871:21, 6879:23, 6880:19, 6880:21, 6887:15, 6887:19, 6888:13, 6892:2, 6898:20, 6901:18, 6902:20, 6906:1, 6917:10, 6918:4, 6918:23, 6918:25, 6919:3, 6919:5, 6919:7, 6923:15, 6924:2, 6940:21, 6941:15, 6944:18, 6944:19, 6945:4, 6950:10</p> <p>consumers [25] - 6781:21, 6794:1, 6806:23, 6812:18, 6819:16, 6862:9, 6863:3, 6863:14, 6878:24, 6880:5, 6880:18, 6880:25, 6883:24, 6887:17, 6887:25, 6899:5, 6902:22, 6902:24, 6904:2, 6905:1, 6919:12, 6919:21, 6919:24, 6950:15, 6960:23</p> <p>contagion [2] - 6906:16, 6906:17</p> <p>contains [1] - 6777:2</p> <p>contemporaneous [7] - 6845:11, 6845:13, 6845:21, 6847:14, 6889:7, 6923:20, 6937:12</p> <p>contend [1] - 6871:23</p> <p>contends [1] - 6870:6</p> <p>context [8] - 6807:18, 6818:25, 6823:22, 6841:15, 6874:8, 6874:17, 6927:1, 6930:16</p> <p>contiguous [1] - 6777:12</p> <p>Continental [26] - 6824:2, 6842:15, 6842:24, 6843:3, 6845:1, 6845:3, 6845:4, 6845:6, 6845:10, 6845:16, 6845:22, 6846:1, 6846:5, 6846:14, 6846:16, 6847:9, 6848:10, 6848:20, 6848:22, 6848:24, 6849:2, 6849:5, 6849:14, 6850:3, 6904:18, 6937:10</p> <p>continue [9] - 6845:1, 6845:18, 6903:7, 6907:4, 6916:25, 6937:18, 6954:23, 6956:6, 6957:10</p> <p>Continued [4] - 6802:24, 6826:20, 6864:12, 6943:6</p> <p>continued [11] - 6812:22, 6840:19, 6840:24, 6841:5, 6855:12, 6895:14, 6911:21, 6922:20, 6927:7, 6940:3, 6957:18</p> <p>Continuing [2] - 6823:8, 6856:1</p> <p>CONTINUING [2] - 6813:1, 6923:1</p> <p>continuous [1] - 6941:12</p> <p>contract [2] - 6849:6, 6858:6</p> <p>contractual [1] - 6849:22</p> <p>contradict [1] - 6881:15</p>	<p>contradicted [1] - 6890:18</p> <p>contrary [3] - 6845:2, 6880:2, 6930:2</p> <p>contribution [2] - 6829:10, 6855:6</p> <p>contributions [2] - 6828:23, 6829:3</p> <p>control [4] - 6792:13, 6846:10, 6898:2, 6915:9</p> <p>controlled [1] - 6932:7</p> <p>convenience [1] - 6919:11</p> <p>convince [1] - 6936:9</p> <p>copies [1] - 6865:7</p> <p>copy [1] - 6776:20</p> <p>copying [1] - 6898:12</p> <p>Corbett [3] - 6836:10, 6836:21, 6857:13</p> <p>core [6] - 6783:19, 6803:1, 6826:13, 6826:16, 6827:15, 6963:19</p> <p>corporate [16] - 6832:14, 6833:10, 6833:15, 6834:21, 6834:22, 6834:25, 6835:4, 6835:5, 6835:14, 6835:20, 6836:24, 6838:3, 6854:19, 6928:5, 6928:7, 6933:10</p> <p>corporation [10] - 6818:7, 6822:3, 6833:14, 6834:21, 6835:1, 6835:7, 6836:3, 6836:24, 6836:25, 6938:19</p> <p>corporations [7] - 6833:9, 6835:15, 6836:3, 6836:10, 6836:23, 6837:11, 6935:7</p> <p>correct [11] - 6798:5, 6799:3, 6801:22, 6827:5, 6853:16, 6853:19, 6910:15, 6915:15, 6941:11, 6945:19, 6948:9</p> <p>correction [2] - 6790:5, 6790:12</p> <p>cost [24] - 6781:4, 6782:22, 6782:24, 6786:7, 6787:4, 6791:19, 6812:5, 6820:7, 6829:5, 6841:24, 6841:25, 6842:10, 6842:24, 6843:3, 6844:1, 6844:10, 6844:15, 6863:1, 6863:5, 6925:16, 6926:10, 6926:14, 6926:25</p> <p>costs [13] - 6780:21, 6792:13, 6812:6, 6812:9, 6828:14, 6828:23, 6829:13, 6855:8, 6858:25, 6863:13, 6863:17, 6863:19, 6939:3</p> <p>Cotark [1] - 6948:18</p> <p>Cote [2] - 6948:13, 6948:24</p> <p>coterminous [1] - 6965:23</p> <p>couches [1] - 6885:11</p> <p>Counsel [2] - 6774:6, 6779:19</p> <p>count [1] - 6898:3</p> <p>counties [1] - 6951:25</p> <p>counting [2] - 6779:8</p> <p>country [8] - 6819:20, 6852:9, 6853:7, 6893:21, 6914:14, 6940:24, 6955:2, 6964:18</p> <p>counts [1] - 6852:17</p> <p>couple [10] - 6809:4, 6809:5, 6820:16, 6823:12, 6839:24, 6840:9, 6841:12, 6850:15, 6949:6, 6949:7</p> <p>courage [1] - 6890:6</p> <p>course [14] - 6777:9, 6778:15, 6790:17, 6791:4, 6796:3, 6804:18, 6804:21, 6820:16, 6834:10, 6841:2, 6851:10, 6858:3, 6892:2, 6955:14</p> <p>COURT [153] - 6772:1, 6774:4, 6774:9,</p>	<p>6774:21, 6775:15, 6775:18, 6776:2, 6776:5, 6776:11, 6776:14, 6776:17, 6776:20, 6776:24, 6777:4, 6777:9, 6777:16, 6777:22, 6778:3, 6778:7, 6778:22, 6778:24, 6779:3, 6779:14, 6779:17, 6780:4, 6788:3, 6789:5, 6790:1, 6790:9, 6791:9, 6796:10, 6796:19, 6796:21, 6796:24, 6797:8, 6797:11, 6797:13, 6797:19, 6801:23, 6802:9, 6802:11, 6802:15, 6808:6, 6808:25, 6809:6, 6809:9, 6809:11, 6809:13, 6809:18, 6809:22, 6813:21, 6814:1, 6814:3, 6814:6, 6814:9, 6814:13, 6816:2, 6816:4, 6818:2, 6818:5, 6818:18, 6818:21, 6818:24, 6821:23, 6822:15, 6822:20, 6822:23, 6823:4, 6823:19, 6831:7, 6833:8, 6833:19, 6833:22, 6834:1, 6834:8, 6839:19, 6840:8, 6840:13, 6841:14, 6841:21, 6846:5, 6847:3, 6847:22, 6847:25, 6862:16, 6864:7, 6865:3, 6865:9, 6865:12, 6865:15, 6865:21, 6866:2, 6866:4, 6875:9, 6885:16, 6885:25, 6886:17, 6886:23, 6890:25, 6891:2, 6891:4, 6891:7, 6891:12, 6898:25, 6909:16, 6914:21, 6915:1, 6915:2, 6915:5, 6915:15, 6925:4, 6938:14, 6938:17, 6938:24, 6946:15, 6946:18, 6946:22, 6946:24, 6947:12, 6947:15, 6947:25, 6948:13, 6948:16, 6948:19, 6948:23, 6949:3, 6949:6, 6949:9, 6949:12, 6949:15, 6949:18, 6949:23, 6952:25, 6953:2, 6954:2, 6954:19, 6955:5, 6955:9, 6955:15, 6955:18, 6956:3, 6956:6, 6956:25, 6961:5, 6961:8, 6961:10, 6961:19, 6962:3, 6966:17, 6966:21, 6966:24, 6967:1, 6967:4</p> <p>Court's [1] - 6777:13</p> <p>courtesies [2] - 6778:14, 6967:3</p> <p>Courthouse [1] - 6772:9</p> <p>courtroom [10] - 6774:2, 6806:17, 6809:16, 6820:25, 6823:2, 6880:5, 6890:4, 6890:10, 6910:15, 6923:4</p> <p>COURTROOM [3] - 6774:3, 6774:5, 6823:3</p> <p>courts [3] - 6803:15, 6810:3, 6918:20</p> <p>Courts [1] - 6824:12</p> <p>cover [3] - 6797:13, 6800:18, 6885:19</p> <p>coverage [2] - 6799:20, 6854:16</p> <p>covered [3] - 6895:4, 6912:13, 6949:21</p> <p>covering [1] - 6957:6</p> <p>CRAIG [1] - 6773:4</p> <p>Craig [1] - 6774:8</p> <p>Crate [1] - 6834:21</p> <p>CRAVATH [1] - 6773:11</p> <p>cream [2] - 6927:19, 6927:20</p> <p>create [3] - 6846:8, 6871:3, 6892:5</p> <p>creation [2] - 6961:23</p> <p>credibility [1] - 6933:18</p> <p>credible [2] - 6880:9, 6880:10</p>
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<p>credibly [1] - 6880:6</p> <p>credit [103] - 6780:12, 6781:6, 6782:1, 6782:20, 6782:21, 6782:22, 6782:24, 6783:1, 6783:3, 6785:12, 6786:2, 6790:4, 6790:23, 6793:14, 6798:6, 6798:21, 6799:20, 6800:19, 6804:9, 6804:17, 6804:23, 6805:9, 6806:7, 6807:3, 6807:14, 6807:24, 6808:15, 6812:7, 6812:9, 6812:19, 6813:9, 6816:10, 6824:15, 6824:20, 6825:12, 6826:6, 6826:10, 6826:13, 6826:14, 6826:15, 6826:16, 6827:3, 6827:6, 6827:8, 6827:13, 6827:16, 6827:17, 6827:22, 6831:4, 6832:1, 6832:10, 6833:9, 6834:23, 6835:13, 6836:16, 6857:19, 6862:24, 6863:5, 6863:7, 6863:9, 6863:11, 6863:17, 6880:12, 6880:14, 6914:5, 6914:9, 6914:12, 6914:23, 6915:23, 6916:14, 6916:25, 6917:5, 6918:4, 6918:14, 6919:10, 6919:13, 6919:23, 6920:6, 6921:4, 6921:14, 6921:20, 6922:5, 6923:23, 6924:3, 6924:20, 6957:7, 6962:1, 6962:13, 6962:22, 6963:3, 6963:5, 6963:12, 6963:17, 6963:20, 6963:24, 6964:1, 6964:3, 6964:8</p> <p>critical [9] - 6781:14, 6794:11, 6863:7, 6867:7, 6867:23, 6881:24, 6882:2, 6919:4, 6919:10</p> <p>critically [1] - 6956:19</p> <p>criticism [4] - 6829:14, 6829:16, 6830:3, 6830:4</p> <p>criticisms [1] - 6828:8</p> <p>criticize [1] - 6800:22</p> <p>cropped [2] - 6877:15, 6878:3</p> <p>cross [1] - 6869:5</p> <p>cross-examination [1] - 6869:5</p> <p>cumulative [1] - 6840:4</p> <p>current [9] - 6787:23, 6788:7, 6788:22, 6791:13, 6792:23, 6813:20, 6814:15, 6957:13, 6957:16</p> <p>customer [28] - 6813:8, 6813:10, 6813:14, 6813:15, 6813:16, 6813:18, 6813:19, 6813:21, 6813:22, 6814:14, 6814:16, 6814:20, 6814:23, 6814:25, 6835:16, 6835:17, 6839:2, 6839:22, 6856:23, 6863:4, 6868:10, 6906:23, 6906:24, 6907:5, 6911:7, 6916:4, 6963:22</p> <p>customer's [2] - 6907:2, 6916:3</p> <p>customers [68] - 6781:10, 6784:13, 6784:16, 6784:25, 6785:1, 6786:14, 6786:17, 6795:2, 6795:3, 6807:25, 6808:1, 6812:7, 6812:8, 6813:4, 6813:6, 6814:11, 6814:16, 6815:24, 6826:13, 6826:16, 6827:15, 6828:1, 6831:24, 6832:4, 6836:14, 6836:19, 6837:6, 6837:14, 6837:25, 6839:4, 6839:23, 6846:17, 6854:23, 6856:22, 6857:2, 6857:14, 6858:2, 6858:11, 6863:3, 6863:6, 6863:16, 6875:14, 6881:8, 6902:7, 6909:24, 6910:4,</p>	<p>6910:7, 6910:10, 6910:16, 6911:1, 6911:2, 6911:6, 6911:22, 6916:7, 6918:7, 6920:18, 6935:16, 6937:25, 6940:18, 6941:17, 6945:15, 6962:19, 6962:20, 6962:21, 6963:12, 6963:19, 6963:23</p> <p>cut [9] - 6785:13, 6788:25, 6795:11, 6795:22, 6837:13, 6861:21, 6889:21, 6906:4, 6952:6</p> <p>cuts [1] - 6784:7</p> <p>cutting [5] - 6785:14, 6785:16, 6800:6, 6951:9, 6952:8</p> <p>CVS [1] - 6911:7</p> <p>cycle [2] - 6901:14, 6901:18</p> <p>cynical [1] - 6925:7</p>	<p>debit's [1] - 6824:21</p> <p>debits [1] - 6827:7</p> <p>decade [1] - 6939:15</p> <p>decades [1] - 6902:16</p> <p>decide [6] - 6806:8, 6859:16, 6927:23, 6953:12, 6953:13, 6953:14</p> <p>decided [9] - 6789:6, 6795:12, 6798:6, 6803:8, 6870:4, 6870:10, 6873:12, 6885:18, 6887:12</p> <p>deciding [2] - 6860:5, 6908:18</p> <p>decimal [1] - 6910:8</p> <p>decision [10] - 6779:6, 6779:21, 6779:23, 6849:14, 6849:18, 6877:8, 6909:20, 6916:8, 6966:10</p> <p>decisions [3] - 6811:3, 6839:9, 6843:8</p> <p>deck [2] - 6865:6, 6875:5</p> <p>decline [4] - 6940:2, 6940:3, 6941:16</p> <p>declined [1] - 6904:20</p> <p>declining [1] - 6798:23</p> <p>decrease [1] - 6884:16</p> <p>decreased [1] - 6924:20</p> <p>decreasing [2] - 6877:21, 6877:23</p> <p>decree [2] - 6887:5, 6941:24</p> <p>deduct [1] - 6926:24</p> <p>defeat [3] - 6824:18, 6824:20, 6963:11</p> <p>defend [2] - 6860:11, 6899:8</p> <p>Defendant [1] - 6773:11</p> <p>defendant [5] - 6811:15, 6858:23, 6858:24, 6860:2, 6913:3</p> <p>defendant's [1] - 6899:23</p> <p>defendants [4] - 6821:14, 6821:15, 6860:1, 6950:10</p> <p>Defendants [1] - 6772:13</p> <p>defendants' [1] - 6876:1</p> <p>defended [2] - 6819:3, 6928:15</p> <p>defense [8] - 6796:13, 6819:9, 6819:23, 6864:9, 6865:16, 6868:24, 6873:14, 6873:24</p> <p>Defense [3] - 6776:12, 6776:21, 6966:19</p> <p>defense's [1] - 6966:18</p> <p>defenses [4] - 6782:8, 6782:10, 6782:12, 6838:9</p> <p>defensible [1] - 6927:10</p> <p>deficit [2] - 6903:12, 6933:9</p> <p>deficits [1] - 6903:3</p> <p>defies [1] - 6809:1</p> <p>define [7] - 6804:5, 6807:5, 6825:3, 6828:3, 6858:14, 6925:21, 6926:7</p> <p>defined [2] - 6805:3, 6825:9</p> <p>defining [6] - 6829:17, 6838:7, 6859:5, 6916:20, 6925:13, 6964:2</p> <p>definitely [1] - 6952:25</p> <p>definition [26] - 6802:21, 6804:1, 6804:2, 6804:5, 6804:7, 6804:12, 6804:15, 6806:24, 6807:12, 6823:21, 6824:3, 6824:6, 6824:11, 6825:5, 6825:18, 6832:19, 6838:8, 6838:12, 6878:22, 6912:5, 6912:11, 6912:24, 6913:10, 6925:25, 6964:14, 6965:2</p> <p>definitive [2] - 6821:24, 6822:9</p>
D		
<p>Dallas [2] - 6830:18, 6830:20</p> <p>damage [1] - 6938:6</p> <p>damages [2] - 6896:11, 6896:12</p> <p>Dan [1] - 6866:21</p> <p>danger [5] - 6791:4, 6791:6, 6799:6, 6814:7</p> <p>dark [1] - 6863:6</p> <p>darn [1] - 6885:9</p> <p>dashed [1] - 6853:15</p> <p>Data [3] - 6881:23, 6882:1, 6932:19</p> <p>data [8] - 6895:2, 6905:24, 6919:19, 6919:22, 6920:16, 6920:25, 6924:12, 6924:13</p> <p>database [1] - 6920:18</p> <p>date [1] - 6937:21</p> <p>daunting [1] - 6929:23</p> <p>DC [3] - 6773:4, 6948:9, 6948:10</p> <p>deal [14] - 6795:20, 6809:25, 6836:18, 6837:1, 6837:13, 6845:23, 6845:24, 6846:5, 6847:13, 6852:21, 6853:4, 6858:3, 6867:18, 6904:21</p> <p>dealing [2] - 6873:17, 6965:13</p> <p>deals [5] - 6805:20, 6805:21, 6805:22, 6828:21, 6836:13</p> <p>death [1] - 6890:1</p> <p>debit [74] - 6812:10, 6824:1, 6824:20, 6824:21, 6825:24, 6825:25, 6826:6, 6827:16, 6868:11, 6880:14, 6882:1, 6884:7, 6884:11, 6893:7, 6912:7, 6912:8, 6912:24, 6912:25, 6913:7, 6914:8, 6915:5, 6915:21, 6915:23, 6917:5, 6917:6, 6917:20, 6918:5, 6918:7, 6918:14, 6918:17, 6918:18, 6919:10, 6919:13, 6919:23, 6920:2, 6920:5, 6920:15, 6921:3, 6921:6, 6921:7, 6921:9, 6921:14, 6921:20, 6922:5, 6922:12, 6922:13, 6922:14, 6922:18, 6923:7, 6923:10, 6923:13, 6923:16, 6923:22, 6923:25, 6924:3, 6924:21, 6931:16, 6961:6, 6961:13, 6961:25, 6962:13, 6962:17, 6962:19, 6962:20, 6962:22, 6963:4, 6963:12, 6963:17, 6964:4, 6964:5, 6964:7</p> <p>Debit [1] - 6918:13</p>		

<p>defused [1] - 6794:10</p> <p>degree [1] - 6872:22</p> <p>deliver [3] - 6843:24, 6888:23, 6888:24</p> <p>delivered [2] - 6887:8, 6889:7</p> <p>delivering [3] - 6861:19, 6936:17, 6939:10</p> <p>Dell [1] - 6936:20</p> <p>Delta [19] - 6834:14, 6834:15, 6834:16, 6843:7, 6843:15, 6843:16, 6843:17, 6843:24, 6851:24, 6852:4, 6852:12, 6852:13, 6852:20, 6853:1, 6853:2, 6853:16, 6915:2</p> <p>Delta's [1] - 6834:14</p> <p>demand [12] - 6825:11, 6825:12, 6861:15, 6880:15, 6880:16, 6918:25, 6919:1, 6919:3, 6923:10, 6939:6</p> <p>demonstrate [2] - 6892:8, 6896:7</p> <p>demonstrated [4] - 6862:25, 6863:21, 6911:10, 6944:11</p> <p>demonstrates [1] - 6905:11</p> <p>demonstration [1] - 6876:1</p> <p>denied [2] - 6813:19, 6813:21</p> <p>Dental [1] - 6875:5</p> <p>dentist [1] - 6874:11</p> <p>Dentists [2] - 6800:24, 6801:1</p> <p>dentists [1] - 6951:25</p> <p>denying [3] - 6847:11, 6863:3, 6863:7</p> <p>departed [1] - 6915:9</p> <p>Department [6] - 6773:2, 6831:10, 6868:17, 6885:18, 6886:1, 6954:17</p> <p>department [1] - 6946:19</p> <p>departs [1] - 6915:13</p> <p>dependent [3] - 6831:4, 6831:5, 6835:22</p> <p>deposed [1] - 6866:22</p> <p>deposition [1] - 6903:25</p> <p>Depot [1] - 6782:22</p> <p>DEPUTY [3] - 6774:3, 6774:5, 6823:3</p> <p>derived [2] - 6825:12, 6918:25</p> <p>described [3] - 6811:8, 6874:14, 6893:22</p> <p>describes [3] - 6804:17, 6806:17, 6875:7</p> <p>describing [1] - 6806:18</p> <p>description [3] - 6903:18, 6903:19, 6918:24</p> <p>designed [2] - 6783:16, 6904:11</p> <p>desired [1] - 6960:23</p> <p>despite [1] - 6933:24</p> <p>destroyed [1] - 6889:5</p> <p>destroying [1] - 6937:9</p> <p>detail [1] - 6962:10</p> <p>determination [1] - 6900:1</p> <p>detrimental [3] - 6876:24, 6900:17, 6907:4</p> <p>developed [2] - 6794:25, 6795:4</p> <p>developing [2] - 6794:3, 6902:16</p> <p>developments [1] - 6790:21</p> <p>device [1] - 6792:4</p> <p>diagram [1] - 6901:10</p> <p>dictate [2] - 6810:16, 6861:11</p>	<p>dictating [1] - 6789:16</p> <p>die [2] - 6894:6, 6894:7</p> <p>diesel [1] - 6783:2</p> <p>differ [1] - 6897:9</p> <p>difference [6] - 6784:24, 6788:8, 6788:10, 6795:2, 6831:16, 6907:19</p> <p>different [52] - 6784:19, 6784:20, 6784:21, 6788:4, 6790:4, 6791:3, 6807:3, 6807:5, 6808:23, 6810:5, 6810:13, 6828:12, 6828:13, 6830:4, 6830:12, 6830:17, 6830:22, 6833:5, 6833:9, 6834:23, 6836:6, 6861:13, 6866:12, 6891:24, 6894:3, 6897:5, 6904:15, 6907:1, 6920:10, 6920:22, 6922:15, 6924:16, 6925:19, 6925:20, 6925:23, 6925:25, 6926:7, 6926:8, 6926:11, 6926:12, 6926:21, 6926:22, 6926:23, 6931:22, 6931:25, 6932:25, 6964:19, 6964:24, 6965:10</p> <p>differential [1] - 6799:25</p> <p>differentiate [2] - 6790:22, 6792:21</p> <p>differentiated [16] - 6812:12, 6822:19, 6859:10, 6860:8, 6860:17, 6860:19, 6860:20, 6860:22, 6860:23, 6860:24, 6861:2, 6862:1, 6867:8, 6867:19, 6897:9, 6897:12</p> <p>differentiating [1] - 6898:16</p> <p>differentiation [3] - 6870:1, 6935:15, 6944:8</p> <p>differently [1] - 6859:8</p> <p>difficult [4] - 6790:10, 6937:18, 6937:19, 6961:3</p> <p>diffuse [1] - 6831:23</p> <p>digits [1] - 6910:20</p> <p>diminish [1] - 6843:9</p> <p>diminished [1] - 6899:8</p> <p>diminution [2] - 6842:18, 6843:14</p> <p>dinner [1] - 6926:5</p> <p>dipped [1] - 6946:19</p> <p>direct [23] - 6786:5, 6787:6, 6787:7, 6787:8, 6787:12, 6793:9, 6794:20, 6795:24, 6800:7, 6801:2, 6807:22, 6808:9, 6808:10, 6813:6, 6871:18, 6951:17, 6952:5, 6952:12, 6952:17, 6953:5, 6953:6, 6959:14, 6964:13</p> <p>direction [2] - 6870:18, 6954:14</p> <p>directly [9] - 6793:15, 6794:1, 6805:22, 6823:5, 6826:2, 6834:17, 6837:18, 6861:9, 6940:13</p> <p>directors [1] - 6804:22</p> <p>directory [1] - 6865:24</p> <p>dirt [1] - 6927:8</p> <p>disagree [2] - 6878:13, 6878:15</p> <p>disappear [1] - 6821:18</p> <p>disappearing [1] - 6842:6</p> <p>disappears [1] - 6954:8</p> <p>disappoint [1] - 6909:23</p> <p>disappointed [1] - 6818:23</p> <p>disbelief [1] - 6821:3</p> <p>discipline [1] - 6917:21</p> <p>disclosed [1] - 6863:2</p>	<p>discount [23] - 6780:12, 6781:6, 6782:2, 6788:9, 6801:25, 6814:12, 6814:17, 6818:8, 6851:14, 6852:18, 6868:6, 6869:24, 6895:9, 6896:20, 6901:14, 6921:23, 6925:20, 6933:21, 6936:16, 6940:2, 6940:3, 6944:6, 6954:15</p> <p>discounts [2] - 6857:17, 6866:25</p> <p>discover [5] - 6786:7, 6793:5, 6907:25, 6909:9, 6946:5</p> <p>Discover [38] - 6781:2, 6785:25, 6786:20, 6787:2, 6787:24, 6788:2, 6813:13, 6814:4, 6819:25, 6820:6, 6837:5, 6858:1, 6860:18, 6860:19, 6861:7, 6867:11, 6883:7, 6883:23, 6892:11, 6892:12, 6892:14, 6892:15, 6893:1, 6893:17, 6907:8, 6907:23, 6909:8, 6909:9, 6910:12, 6910:16, 6910:20, 6911:4, 6930:17, 6945:25, 6946:6, 6950:13</p> <p>discover's [1] - 6860:24</p> <p>Discover's [9] - 6786:4, 6787:10, 6787:16, 6787:18, 6800:8, 6800:9, 6860:23, 6892:18, 6952:15</p> <p>discovered [1] - 6810:8</p> <p>discriminate [1] - 6944:9</p> <p>discriminating [1] - 6926:11</p> <p>discrimination [10] - 6827:20, 6828:10, 6828:15, 6829:4, 6829:6, 6838:7, 6925:14, 6925:15, 6945:2, 6945:9</p> <p>discuss [3] - 6783:5, 6783:11, 6841:14</p> <p>discussed [4] - 6841:16, 6948:17, 6949:20, 6966:1</p> <p>discusses [1] - 6937:15</p> <p>discussion [4] - 6823:14, 6946:18, 6962:8, 6964:10</p> <p>discussions [1] - 6779:25</p> <p>dismissed [1] - 6900:22</p> <p>disparage [1] - 6944:11</p> <p>disparaging [1] - 6886:17</p> <p>disparity [1] - 6917:1</p> <p>displayed [1] - 6942:11</p> <p>displays [1] - 6904:3</p> <p>dispositive [1] - 6900:7</p> <p>disprove [2] - 6815:22, 6815:25</p> <p>dispute [7] - 6823:25, 6845:5, 6853:25, 6878:19, 6891:22, 6950:20, 6964:5</p> <p>disrupt [6] - 6784:2, 6784:5, 6811:5, 6872:10, 6873:18, 6951:18</p> <p>disrupted [3] - 6787:3, 6873:2, 6873:8</p> <p>disrupting [1] - 6877:3</p> <p>disruption [1] - 6951:8</p> <p>disruptive [1] - 6794:14</p> <p>disrupts [1] - 6873:11</p> <p>distinction [2] - 6919:10, 6919:14</p> <p>distinguishing [1] - 6965:19</p> <p>DISTRICT [2] - 6772:1, 6772:1</p> <p>District [4] - 6772:20, 6783:23, 6877:16, 6950:7</p> <p>divine [1] - 6886:1</p> <p>DIVISION [1] - 6773:2</p> <p>division [2] - 6828:20, 6829:22</p>
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<p>document [17] - 6804:21, 6828:18, 6828:19, 6829:20, 6829:22, 6829:23, 6840:8, 6845:15, 6845:21, 6847:14, 6889:9, 6898:11, 6905:9, 6937:12, 6937:14, 6937:15</p> <p>documents [5] - 6845:14, 6847:8, 6909:5, 6923:20, 6946:1</p> <p>dog [1] - 6935:17</p> <p>dollar [1] - 6816:19</p> <p>dollars [3] - 6926:5, 6931:5, 6935:5</p> <p>domestic [5] - 6840:22, 6851:18, 6851:19, 6880:8, 6880:11</p> <p>dominant [1] - 6867:18</p> <p>dominated [2] - 6902:17, 6935:18</p> <p>DONALD [1] - 6773:17</p> <p>Donald [1] - 6775:5</p> <p>done [17] - 6776:4, 6796:12, 6802:2, 6802:5, 6810:6, 6871:20, 6874:24, 6878:14, 6891:17, 6898:10, 6905:20, 6908:22, 6912:12, 6916:9, 6916:10, 6925:2, 6939:20</p> <p>donut [1] - 6929:1</p> <p>Donuts [1] - 6911:20</p> <p>door [3] - 6837:6, 6944:22, 6944:24</p> <p>doubt [2] - 6896:19, 6948:3</p> <p>Dow [2] - 6934:20, 6934:21</p> <p>down [52] - 6789:4, 6795:13, 6803:18, 6804:25, 6817:20, 6819:5, 6819:6, 6819:7, 6820:2, 6820:11, 6820:13, 6820:14, 6841:19, 6843:5, 6851:1, 6851:5, 6851:10, 6853:14, 6869:25, 6870:2, 6876:12, 6876:14, 6876:18, 6881:4, 6882:21, 6882:25, 6885:9, 6887:10, 6888:13, 6894:23, 6894:24, 6895:11, 6895:13, 6896:19, 6896:21, 6897:24, 6897:25, 6906:3, 6906:4, 6908:10, 6914:18, 6927:23, 6931:16, 6941:14, 6942:2, 6944:7, 6944:8, 6945:14, 6958:2, 6963:25</p> <p>dozen [1] - 6894:15</p> <p>Dr [27] - 6869:4, 6869:23, 6871:25, 6872:19, 6881:21, 6881:22, 6882:18, 6884:6, 6887:8, 6887:20, 6892:1, 6894:21, 6905:18, 6905:19, 6913:21, 6915:22, 6919:18, 6924:24, 6924:25, 6925:15, 6935:16, 6938:13, 6941:25, 6944:6, 6945:14, 6953:19</p> <p>dramatic [3] - 6822:8, 6890:14, 6894:23</p> <p>dramatically [6] - 6816:8, 6850:18, 6866:12, 6894:3, 6897:9, 6932:25</p> <p>draw [4] - 6827:10, 6881:3, 6882:3, 6885:7</p> <p>drawers [1] - 6929:2</p> <p>drawing [2] - 6821:20, 6882:8</p> <p>drew [2] - 6889:8, 6889:10</p> <p>drifting [1] - 6894:24</p> <p>drive [2] - 6902:6, 6958:24</p> <p>driven [5] - 6849:15, 6898:9, 6925:8, 6940:20, 6940:22</p> <p>driving [2] - 6849:18, 6939:6</p> <p>drop [8] - 6827:3, 6827:15, 6849:6,</p>	<p>6941:17, 6942:20, 6942:22, 6962:13, 6963:17</p> <p>drop-off [1] - 6941:17</p> <p>due [2] - 6866:1, 6965:12</p> <p>dumb [1] - 6940:7</p> <p>Dunkin' [1] - 6911:20</p> <p>duopoly [5] - 6796:3, 6893:5, 6954:7, 6954:9, 6954:10</p> <p>duplicating [1] - 6903:16</p> <p>durability [1] - 6944:2</p> <p>durable [1] - 6944:3</p> <p>Durban [1] - 6884:7</p> <p>Durbin [2] - 6924:18, 6962:6</p> <p>during [11] - 6777:10, 6813:8, 6820:21, 6851:5, 6853:21, 6858:2, 6866:16, 6903:23, 6917:20, 6919:18, 6920:9</p> <p>DX [1] - 6905:10</p> <p>dynamic [1] - 6788:23</p>	<p>6965:16</p> <p>effective [1] - 6936:16</p> <p>effectively [1] - 6836:11</p> <p>effects [33] - 6783:12, 6783:22, 6785:3, 6794:15, 6801:2, 6801:16, 6801:17, 6804:3, 6807:19, 6811:16, 6811:18, 6869:2, 6869:3, 6874:19, 6876:24, 6899:15, 6899:18, 6900:2, 6903:4, 6903:7, 6911:11, 6911:13, 6911:16, 6929:12, 6930:1, 6930:3, 6930:10, 6936:24, 6951:13, 6965:11, 6965:14, 6965:19</p> <p>efficient [3] - 6793:1, 6960:3, 6960:9</p> <p>efficiently [2] - 6823:11, 6823:18</p> <p>effort [1] - 6864:5</p> <p>efforts [2] - 6933:24, 6935:23</p> <p>eggs [1] - 6946:5</p> <p>eight [4] - 6906:3, 6923:16, 6924:20, 6936:13</p> <p>eighteen [1] - 6901:23</p> <p>Eighth [1] - 6773:12</p> <p>eighty [2] - 6898:3, 6911:2</p> <p>eighty-five [1] - 6911:2</p> <p>either [6] - 6812:10, 6893:6, 6902:24, 6921:7, 6947:22, 6954:11</p> <p>elaborate [1] - 6951:16</p> <p>electronic [2] - 6777:1, 6792:6</p> <p>electronically [1] - 6865:5</p> <p>element [2] - 6839:18, 6854:7</p> <p>elements [1] - 6838:23</p> <p>elevator [1] - 6927:18</p> <p>elicited [1] - 6862:21</p> <p>eliminate [3] - 6869:12, 6869:23, 6869:25</p> <p>eliminated [2] - 6870:19, 6900:6</p> <p>elsewhere [4] - 6854:17, 6907:8, 6924:15, 6932:21</p> <p>embarrassment [2] - 6856:12, 6856:15</p> <p>embrace [1] - 6871:7</p> <p>embraces [2] - 6874:1, 6874:18</p> <p>emphasize [1] - 6817:7</p> <p>emphasized [1] - 6867:7</p> <p>empirical [4] - 6787:13, 6801:9, 6875:25, 6905:7</p> <p>employees [7] - 6782:25, 6833:14, 6834:22, 6834:25, 6835:8, 6957:3, 6957:4</p> <p>enables [2] - 6816:12, 6818:16</p> <p>enactment [1] - 6864:2</p> <p>encourage [7] - 6786:17, 6788:21, 6792:16, 6795:2, 6795:3, 6836:19, 6901:18</p> <p>end [8] - 6777:17, 6795:11, 6825:14, 6868:15, 6877:25, 6902:9, 6940:9, 6954:23</p> <p>ended [2] - 6795:24, 6840:6</p> <p>endpoint [1] - 6919:1</p> <p>enforce [1] - 6863:22</p> <p>enforcement [2] - 6808:3, 6864:2</p> <p>enforces [1] - 6785:10</p> <p>enforcing [1] - 6868:2</p>
E		
<p>earliest [1] - 6851:22</p> <p>early [2] - 6777:19, 6794:24</p> <p>earn [4] - 6819:2, 6819:8, 6832:15, 6915:17</p> <p>earned [1] - 6926:18</p> <p>easily [2] - 6955:19, 6956:11</p> <p>East [1] - 6772:23</p> <p>EASTERN [1] - 6772:1</p> <p>Eastman [1] - 6785:16</p> <p>easy [2] - 6796:17, 6956:12</p> <p>eat [2] - 6848:1, 6848:2</p> <p>economic [6] - 6816:23, 6905:21, 6934:12, 6934:14, 6934:16, 6965:21</p> <p>economically [1] - 6852:15</p> <p>economics [1] - 6875:12</p> <p>economist [4] - 6825:2, 6825:7, 6882:11, 6888:4</p> <p>economists [1] - 6881:1</p> <p>economy [3] - 6784:12, 6798:22, 6960:14</p> <p>Ed [1] - 6828:19</p> <p>effect [86] - 6785:7, 6786:6, 6787:12, 6787:14, 6787:21, 6787:22, 6787:23, 6794:14, 6794:20, 6795:25, 6798:1, 6800:4, 6800:7, 6800:16, 6800:17, 6800:19, 6801:20, 6802:2, 6802:16, 6802:22, 6811:15, 6813:4, 6813:6, 6814:18, 6814:20, 6815:2, 6815:14, 6815:17, 6816:16, 6817:1, 6817:3, 6817:5, 6838:24, 6840:24, 6841:5, 6851:20, 6853:9, 6853:18, 6869:9, 6870:6, 6870:7, 6872:9, 6872:12, 6872:14, 6873:7, 6875:13, 6876:1, 6877:11, 6877:19, 6877:22, 6878:9, 6878:18, 6881:1, 6881:3, 6882:12, 6882:14, 6882:20, 6896:13, 6899:2, 6900:17, 6902:19, 6902:22, 6903:23, 6904:23, 6905:3, 6905:6, 6905:11, 6906:16, 6906:17, 6911:25, 6912:12, 6928:19, 6929:12, 6930:5, 6951:7, 6951:17, 6952:12, 6952:17, 6962:5,</p>		

<p>engage [3] - 6857:1, 6868:25, 6874:14</p> <p>Engineers [1] - 6858:24</p> <p>English [1] - 6889:20</p> <p>enormous [1] - 6898:2</p> <p>enter [1] - 6946:11</p> <p>entered [1] - 6903:5</p> <p>entering [1] - 6948:8</p> <p>enters [2] - 6774:2, 6823:2</p> <p>entertainment [6] - 6797:6, 6799:13, 6799:16, 6889:19, 6925:1, 6925:3</p> <p>Entertainment [11] - 6827:19, 6828:21, 6829:2, 6829:6, 6829:22, 6829:25, 6831:3, 6832:3, 6851:8, 6854:14, 6964:10</p> <p>entire [5] - 6866:16, 6869:10, 6889:22, 6905:5, 6967:3</p> <p>entirely [2] - 6868:23, 6948:4</p> <p>entities [2] - 6804:24, 6857:21</p> <p>entitled [9] - 6808:1, 6808:2, 6808:19, 6819:10, 6820:14, 6896:11, 6939:23, 6957:13, 6957:15</p> <p>entity [1] - 6819:25</p> <p>entrances [1] - 6893:21</p> <p>entry [1] - 6853:25</p> <p>environment [2] - 6789:8, 6796:11</p> <p>equal [1] - 6894:18</p> <p>ERIC [1] - 6773:17</p> <p>Eric [1] - 6775:7</p> <p>erroneous [1] - 6882:9</p> <p>error [2] - 6874:23, 6885:15</p> <p>errors [1] - 6853:16</p> <p>especially [2] - 6791:5, 6797:3</p> <p>essence [4] - 6785:15, 6785:17, 6810:5, 6952:8</p> <p>essential [5] - 6785:2, 6786:10, 6786:12, 6827:9, 6951:8</p> <p>essentially [2] - 6903:6, 6933:15</p> <p>establish [3] - 6811:16, 6816:21, 6842:5</p> <p>established [9] - 6824:7, 6829:21, 6830:2, 6830:15, 6839:18, 6854:10, 6859:12, 6900:3, 6961:12</p> <p>establishes [2] - 6816:21, 6855:10</p> <p>establishing [1] - 6815:1</p> <p>estate [1] - 6816:9</p> <p>estimate [1] - 6908:13</p> <p>estimates [1] - 6891:25</p> <p>et [2] - 6867:22, 6880:14</p> <p>etcetera [1] - 6903:11</p> <p>Ethan [1] - 6774:20</p> <p>ETHAN [1] - 6773:8</p> <p>evaluate [1] - 6956:18</p> <p>evaluating [2] - 6839:6, 6874:4</p> <p>Evan [1] - 6775:1</p> <p>EVAN [1] - 6773:13</p> <p>evaporates [1] - 6935:16</p> <p>event [2] - 6801:15, 6912:3</p> <p>eventually [2] - 6800:12, 6816:25</p> <p>everyday [7] - 6784:12, 6797:23, 6799:12, 6851:9, 6920:24, 6925:23</p> <p>Everyday [1] - 6904:10</p> <p>Everywhere [3] - 6905:21, 6905:22,</p>	<p>6906:3</p> <p>evidence [147] - 6780:9, 6781:5, 6781:8, 6783:6, 6786:5, 6787:6, 6787:7, 6787:8, 6787:12, 6787:13, 6787:14, 6789:21, 6791:5, 6791:12, 6791:13, 6791:17, 6793:3, 6794:5, 6794:12, 6794:14, 6794:16, 6794:20, 6795:17, 6795:24, 6798:19, 6798:20, 6798:25, 6800:11, 6801:9, 6801:12, 6801:14, 6811:22, 6811:24, 6812:15, 6812:20, 6813:3, 6814:22, 6816:11, 6816:14, 6816:21, 6820:22, 6821:8, 6824:10, 6825:15, 6827:2, 6829:18, 6836:2, 6836:6, 6839:8, 6839:12, 6839:17, 6839:25, 6842:4, 6844:23, 6845:2, 6845:12, 6845:14, 6846:4, 6847:20, 6849:4, 6849:17, 6850:4, 6853:23, 6854:25, 6855:2, 6855:3, 6855:5, 6855:6, 6855:10, 6856:3, 6857:21, 6862:21, 6862:25, 6870:6, 6870:22, 6870:23, 6872:16, 6872:17, 6876:7, 6876:15, 6883:9, 6885:3, 6885:24, 6889:25, 6890:1, 6890:18, 6892:17, 6893:12, 6895:10, 6895:11, 6896:3, 6899:23, 6900:5, 6903:21, 6904:16, 6905:7, 6908:11, 6911:4, 6911:5, 6911:16, 6916:18, 6916:22, 6917:3, 6918:12, 6919:4, 6919:8, 6920:7, 6920:12, 6921:3, 6921:5, 6922:4, 6922:15, 6922:17, 6923:6, 6923:11, 6923:13, 6923:14, 6923:15, 6927:6, 6929:14, 6929:20, 6930:7, 6930:12, 6930:13, 6930:14, 6932:22, 6934:3, 6936:6, 6936:19, 6938:25, 6940:6, 6940:7, 6941:10, 6944:12, 6952:12, 6952:17, 6953:16, 6953:18, 6953:24, 6962:6, 6962:12</p> <p>evidence-qua-power [1] - 6929:14</p> <p>evidentiary [1] - 6948:12</p> <p>evolving [1] - 6866:24</p> <p>EWALT [2] - 6773:8, 6774:18</p> <p>Ewalt [1] - 6774:19</p> <p>exact [2] - 6829:8, 6837:20</p> <p>exactly [24] - 6782:6, 6783:17, 6828:18, 6829:23, 6836:15, 6852:12, 6858:3, 6868:9, 6882:7, 6889:8, 6893:23, 6902:14, 6906:11, 6907:18, 6908:21, 6924:21, 6928:16, 6932:10, 6938:21, 6939:11, 6945:23, 6946:3, 6956:23, 6958:18</p> <p>examination [2] - 6869:5, 6905:19</p> <p>examinations [1] - 6913:21</p> <p>examine [1] - 6783:21</p> <p>example [23] - 6786:5, 6794:23, 6813:7, 6814:8, 6837:6, 6837:8, 6839:14, 6842:14, 6844:25, 6873:9, 6879:7, 6904:18, 6904:21, 6911:6, 6911:20, 6917:3, 6932:24, 6948:21, 6948:24, 6963:1, 6965:7, 6965:9</p> <p>examples [9] - 6794:4, 6821:16, 6830:14, 6856:17, 6875:19, 6922:11, 6930:4, 6932:25, 6935:24</p>	<p>exceed [1] - 6863:12</p> <p>exception [2] - 6886:3, 6887:9</p> <p>exceptions [1] - 6851:24</p> <p>excerpt [1] - 6786:13</p> <p>excerpts [1] - 6913:20</p> <p>exchange [3] - 6786:9, 6825:20, 6876:9</p> <p>excited [1] - 6891:7</p> <p>exclude [2] - 6846:13, 6859:21</p> <p>excluded [1] - 6877:25</p> <p>exclusionary [10] - 6867:5, 6877:8, 6877:17, 6887:11, 6887:13, 6887:20, 6887:23, 6903:4, 6903:5, 6950:11</p> <p>Exclusionary [1] - 6901:25</p> <p>exclusive [2] - 6849:11, 6873:17</p> <p>executive [4] - 6821:17, 6821:19, 6862:4, 6866:22</p> <p>executives [3] - 6890:24, 6901:3, 6933:21</p> <p>exercised [1] - 6880:15</p> <p>Exhibit [3] - 6865:10, 6927:24, 6966:19</p> <p>exhibits [1] - 6878:23</p> <p>exist [1] - 6887:4</p> <p>existed [3] - 6796:11, 6800:10, 6801:19</p> <p>existence [1] - 6892:20</p> <p>existing [2] - 6793:9, 6899:17</p> <p>exists [6] - 6824:5, 6871:5, 6878:17, 6878:19, 6880:3, 6951:2</p> <p>expect [9] - 6780:14, 6785:13, 6884:6, 6884:15, 6884:16, 6924:22, 6941:15, 6941:17, 6958:5</p> <p>expected [1] - 6930:9</p> <p>expenses [2] - 6782:21, 6912:2</p> <p>expensive [3] - 6789:11, 6851:7, 6954:15</p> <p>experience [5] - 6786:4, 6879:5, 6906:23, 6906:25</p> <p>experienced [1] - 6841:8</p> <p>experiences [1] - 6905:13</p> <p>experiment [5] - 6883:3, 6883:4, 6891:6, 6923:3, 6931:10</p> <p>expert [14] - 6800:14, 6820:20, 6821:6, 6825:5, 6869:12, 6871:23, 6872:15, 6876:10, 6881:20, 6885:12, 6890:17, 6895:12, 6910:5, 6934:12</p> <p>experts [5] - 6778:21, 6821:4, 6872:1, 6882:25, 6941:13</p> <p>explain [9] - 6787:17, 6793:21, 6796:25, 6812:15, 6812:20, 6815:16, 6884:9, 6932:13, 6938:22</p> <p>explained [18] - 6781:2, 6781:16, 6784:15, 6786:21, 6793:7, 6793:23, 6799:9, 6815:6, 6826:4, 6827:8, 6827:24, 6924:10, 6935:6, 6935:21, 6953:23, 6963:15, 6964:22, 6965:7</p> <p>explaining [5] - 6800:13, 6800:14, 6835:22, 6839:10, 6953:9</p> <p>explains [3] - 6786:13, 6962:11, 6963:15</p> <p>explanation [4] - 6815:13, 6879:1, 6932:15, 6963:18</p> <p>explanations [1] - 6907:11</p>
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<p>explicitly [1] - 6872:11</p> <p>explore [1] - 6793:6</p> <p>express [1] - 6847:10</p> <p>EXPRESS [3] - 6772:10, 6772:10, 6772:15</p> <p>Express [195] - 6773:11, 6775:1, 6775:3, 6775:5, 6775:7, 6775:9, 6775:10, 6775:12, 6775:14, 6775:17, 6778:20, 6779:12, 6779:19, 6780:19, 6785:8, 6793:18, 6798:16, 6801:23, 6810:18, 6812:19, 6813:11, 6813:17, 6815:13, 6819:19, 6820:10, 6820:17, 6821:1, 6821:11, 6821:21, 6823:24, 6825:6, 6825:13, 6825:15, 6826:17, 6828:20, 6829:16, 6831:5, 6835:19, 6835:23, 6837:4, 6837:19, 6839:2, 6839:11, 6839:14, 6839:20, 6841:11, 6842:10, 6842:16, 6842:21, 6842:25, 6843:15, 6843:18, 6843:19, 6843:22, 6844:2, 6844:6, 6844:11, 6844:15, 6844:19, 6844:25, 6845:7, 6845:21, 6846:6, 6846:8, 6846:13, 6846:24, 6847:15, 6848:5, 6848:12, 6849:15, 6849:25, 6850:2, 6850:14, 6850:22, 6852:1, 6852:5, 6852:10, 6852:11, 6852:13, 6852:14, 6852:23, 6853:3, 6853:4, 6853:7, 6854:3, 6854:24, 6855:11, 6856:4, 6856:8, 6856:11, 6856:13, 6856:17, 6858:5, 6858:8, 6858:12, 6859:1, 6859:15, 6859:19, 6859:21, 6861:16, 6862:4, 6864:1, 6865:7, 6866:22, 6867:9, 6867:11, 6867:17, 6867:19, 6867:25, 6872:21, 6879:23, 6881:10, 6881:12, 6881:19, 6883:6, 6883:17, 6883:20, 6884:13, 6884:14, 6885:19, 6889:22, 6890:15, 6890:23, 6892:13, 6892:15, 6897:1, 6897:21, 6901:3, 6902:13, 6902:15, 6902:20, 6903:2, 6903:10, 6904:24, 6906:2, 6907:24, 6908:9, 6910:4, 6911:17, 6911:23, 6911:24, 6914:24, 6916:16, 6916:25, 6917:17, 6919:1, 6921:23, 6922:16, 6923:5, 6923:7, 6924:2, 6925:10, 6925:18, 6925:22, 6926:18, 6927:17, 6929:1, 6932:6, 6932:10, 6933:18, 6934:19, 6935:10, 6935:20, 6936:9, 6936:13, 6938:19, 6942:10, 6942:21, 6942:22, 6944:16, 6945:22, 6946:6, 6946:10, 6946:12, 6950:13, 6954:5, 6954:8, 6954:21, 6955:1, 6955:3, 6955:19, 6955:22, 6956:11, 6956:13, 6958:25, 6959:1, 6959:8, 6959:10, 6959:18, 6960:13, 6961:1, 6962:18</p> <p>Express' [2] - 6785:6, 6901:14</p> <p>Express's [18] - 6783:7, 6783:13, 6784:9, 6798:23, 6799:5, 6825:2, 6840:3, 6841:25, 6850:24, 6852:7, 6854:12, 6862:3, 6878:22, 6906:17, 6910:19, 6913:1, 6921:23, 6922:9</p> <p>expressed [2] - 6780:19, 6783:25</p> <p>expressing [1] - 6924:14</p>	<p>extended [1] - 6778:14</p> <p>extensive [1] - 6955:18</p> <p>extensively [2] - 6953:21, 6953:23</p> <p>extra [1] - 6816:19</p> <p>extraneous [1] - 6861:14</p> <p>extrapolate [1] - 6930:4</p> <p>extreme [6] - 6817:7, 6817:10, 6820:23, 6822:16, 6947:3, 6954:4</p> <p>extremely [1] - 6963:16</p> <p>Exxon [2] - 6801:5, 6876:4</p> <p>eye [1] - 6775:22</p>	<p>fashioned [1] - 6929:15</p> <p>fast [3] - 6833:21, 6918:6, 6926:1</p> <p>fastest [3] - 6921:6, 6921:8, 6921:9</p> <p>fat [1] - 6889:11</p> <p>fatal [2] - 6900:7, 6928:19</p> <p>favor [5] - 6779:9, 6871:10, 6873:13, 6873:24, 6946:12</p> <p>favorable [1] - 6955:13</p> <p>feature [3] - 6805:14, 6904:14, 6965:19</p> <p>features [1] - 6877:20</p> <p>Federal [2] - 6875:6, 6919:8</p> <p>Federation [7] - 6784:1, 6800:24, 6801:1, 6801:6, 6876:19, 6951:11, 6951:23</p> <p>fee [1] - 6900:14</p> <p>fees [16] - 6782:20, 6782:21, 6782:22, 6782:24, 6783:1, 6783:3, 6817:25, 6852:8, 6863:11, 6884:16, 6887:20, 6888:13, 6889:11, 6915:18, 6922:19, 6960:6</p> <p>fellow [1] - 6902:20</p> <p>felt [1] - 6797:25</p> <p>few [16] - 6783:14, 6807:8, 6817:25, 6831:18, 6831:21, 6832:1, 6848:6, 6848:7, 6872:24, 6901:7, 6909:18, 6919:5, 6930:24, 6935:24, 6949:21, 6949:25</p> <p>fewer [1] - 6933:6</p> <p>field [2] - 6879:6, 6931:2</p> <p>fiercely [1] - 6950:12</p> <p>fifteen [3] - 6898:6, 6910:22, 6920:10</p> <p>fifth [2] - 6889:22, 6905:5</p> <p>Fifth [1] - 6773:3</p> <p>fight [2] - 6782:6, 6782:7</p> <p>fighting [3] - 6781:20, 6862:6, 6958:14</p> <p>figure [4] - 6793:8, 6818:15, 6928:18, 6954:13</p> <p>figured [1] - 6799:18</p> <p>figuring [1] - 6835:7</p> <p>filings [1] - 6934:18</p> <p>fill [2] - 6911:7, 6933:23</p> <p>filled [1] - 6909:8</p> <p>final [3] - 6830:4, 6837:8, 6844:19</p> <p>finally [3] - 6793:20, 6815:4, 6850:23</p> <p>finances [1] - 6917:24</p> <p>financial [4] - 6798:13, 6901:15, 6917:21, 6934:16</p> <p>financing [1] - 6935:13</p> <p>findings [3] - 6926:13, 6926:15, 6962:10</p> <p>fine [9] - 6776:5, 6782:16, 6836:12, 6840:13, 6865:21, 6891:18, 6910:6, 6941:4, 6949:23</p> <p>finish [1] - 6909:19</p> <p>firm [7] - 6830:5, 6830:9, 6830:18, 6854:2, 6936:17, 6965:8, 6965:23</p> <p>firms [2] - 6810:13, 6830:11</p> <p>first [33] - 6775:24, 6775:25, 6776:1, 6783:11, 6783:14, 6786:5, 6803:20, 6804:1, 6811:8, 6811:14, 6816:6, 6820:16, 6828:9, 6829:14, 6831:8,</p>
F		
<p>face [20] - 6784:22, 6793:9, 6799:11, 6799:22, 6807:2, 6819:15, 6821:13, 6835:23, 6858:20, 6859:16, 6859:17, 6906:11, 6917:13, 6936:25, 6957:12, 6958:6, 6958:23, 6959:16, 6960:15, 6961:3</p> <p>faced [2] - 6855:1, 6856:3</p> <p>faceless [1] - 6890:8</p> <p>facing [2] - 6819:22, 6863:19</p> <p>fact [72] - 6794:16, 6795:17, 6803:12, 6805:16, 6807:15, 6815:3, 6816:21, 6824:5, 6832:18, 6839:5, 6843:22, 6845:22, 6846:15, 6846:19, 6848:4, 6866:22, 6867:1, 6869:13, 6870:9, 6870:20, 6872:1, 6872:16, 6882:12, 6882:21, 6882:25, 6883:14, 6885:1, 6885:3, 6887:6, 6887:9, 6887:10, 6887:19, 6893:4, 6893:6, 6894:20, 6895:1, 6896:1, 6896:8, 6896:14, 6896:15, 6896:25, 6897:14, 6898:22, 6900:20, 6900:24, 6902:10, 6911:15, 6911:16, 6912:2, 6912:13, 6914:1, 6914:4, 6924:17, 6924:20, 6924:23, 6925:22, 6927:6, 6929:5, 6930:9, 6932:17, 6936:15, 6937:15, 6941:3, 6941:24, 6942:19, 6953:24, 6961:16, 6962:10, 6963:11, 6964:13</p> <p>factors [1] - 6817:24</p> <p>facts [23] - 6785:2, 6790:10, 6801:20, 6803:14, 6812:5, 6829:15, 6857:9, 6866:11, 6868:24, 6870:20, 6871:18, 6873:15, 6887:2, 6887:3, 6888:5, 6888:21, 6892:21, 6900:1, 6908:19, 6908:20, 6909:4</p> <p>factual [8] - 6796:5, 6850:16, 6858:9, 6870:22, 6872:15, 6888:18, 6892:7, 6894:12</p> <p>factually [1] - 6817:17</p> <p>failed [3] - 6811:22, 6899:22, 6900:19</p> <p>fair [5] - 6822:7, 6831:7, 6897:20, 6919:17, 6938:12</p> <p>fairness [1] - 6942:8</p> <p>fall [2] - 6876:11, 6883:1</p> <p>familiar [2] - 6783:8, 6939:14</p> <p>family [2] - 6944:13, 6944:14</p> <p>far [4] - 6801:17, 6810:21, 6850:1, 6866:9</p> <p>Fargo [3] - 6805:20, 6833:13, 6833:15</p>		

<p>6866:6, 6870:15, 6871:12, 6899:4, 6912:9, 6912:19, 6917:16, 6919:7, 6920:22, 6925:6, 6929:16, 6930:15, 6950:1, 6951:12, 6954:20, 6956:5, 6956:9, 6959:6</p> <p>First [2] - 6881:23, 6882:1</p> <p>fit [3] - 6833:11, 6833:16, 6867:1</p> <p>fits [1] - 6961:6</p> <p>five [16] - 6804:24, 6839:15, 6840:6, 6877:10, 6892:14, 6892:18, 6893:16, 6905:12, 6906:2, 6908:3, 6909:1, 6911:2, 6927:20, 6931:21, 6936:8</p> <p>fix [1] - 6882:23</p> <p>fixed [1] - 6912:2</p> <p>fixing [2] - 6874:8, 6874:9</p> <p>FLEXNER [3] - 6773:15, 6773:17, 6775:4</p> <p>Flexner [1] - 6775:5</p> <p>flight [4] - 6843:10, 6843:11, 6965:15, 6965:17</p> <p>Flindon [1] - 6897:18</p> <p>float [1] - 6915:17</p> <p>floating [1] - 6925:11</p> <p>flow [1] - 6806:22</p> <p>flunked [1] - 6936:2</p> <p>fly [4] - 6832:7, 6927:11, 6928:22, 6928:23</p> <p>focus [3] - 6805:25, 6827:18, 6963:20</p> <p>focused [3] - 6947:8, 6948:4, 6960:8</p> <p>focuses [1] - 6916:2</p> <p>focusing [1] - 6882:3</p> <p>follow [4] - 6783:10, 6807:23, 6953:19, 6961:18</p> <p>follow-up [1] - 6953:19</p> <p>following [6] - 6802:24, 6826:20, 6865:2, 6927:11, 6943:6, 6949:14</p> <p>follows [1] - 6808:21</p> <p>food [2] - 6926:1, 6935:17</p> <p>for-everyone-in-the-market [1] - 6914:8</p> <p>force [7] - 6810:10, 6867:20, 6902:15, 6903:12, 6930:20, 6931:7, 6932:9</p> <p>forces [3] - 6790:2, 6863:20, 6903:7</p> <p>foreign [1] - 6891:6</p> <p>foresee [1] - 6901:3</p> <p>foresight [1] - 6939:17</p> <p>forgetting [2] - 6823:13, 6823:16</p> <p>form [18] - 6795:21, 6800:10, 6812:19, 6816:18, 6820:16, 6820:23, 6837:16, 6837:17, 6838:8, 6838:12, 6846:20, 6863:15, 6873:4, 6874:15, 6952:5, 6953:25, 6966:4, 6966:5</p> <p>forms [5] - 6790:23, 6791:7, 6820:16, 6880:12, 6920:18</p> <p>forth [2] - 6871:11, 6920:1</p> <p>fortunate [1] - 6966:10</p> <p>fortune [1] - 6902:15</p> <p>forty [2] - 6922:8, 6922:10</p> <p>forward [3] - 6779:21, 6899:22, 6932:22</p> <p>foster [2] - 6887:24, 6945:8</p> <p>four [24] - 6775:19, 6778:19, 6778:21, 6795:17, 6797:20, 6832:11, 6836:1,</p>	<p>6875:19, 6883:8, 6884:5, 6884:10, 6889:23, 6890:19, 6890:23, 6897:17, 6905:5, 6906:14, 6918:12, 6925:5, 6931:2, 6935:3, 6940:4, 6946:4</p> <p>fourteen [2] - 6867:3, 6906:9</p> <p>fourth [1] - 6933:19</p> <p>frame [2] - 6859:8, 6895:4</p> <p>framework [2] - 6807:21, 6811:12</p> <p>France [1] - 6889:8</p> <p>Francisco [1] - 6933:14</p> <p>Francisco/Miami [1] - 6831:16</p> <p>Frankly [1] - 6909:5</p> <p>frankly [11] - 6798:18, 6819:23, 6820:22, 6839:25, 6850:21, 6851:13, 6852:8, 6853:8, 6866:12, 6866:16, 6901:2</p> <p>free [15] - 6781:10, 6784:17, 6811:2, 6819:17, 6819:21, 6836:18, 6861:25, 6907:25, 6908:1, 6911:13, 6911:14, 6911:23, 6912:1, 6912:3, 6944:9</p> <p>free-riding [4] - 6911:13, 6911:14, 6912:1, 6912:3</p> <p>freedom [3] - 6784:23, 6787:24, 6856:21</p> <p>frequently [1] - 6815:6</p> <p>friendly [1] - 6786:8</p> <p>frivolous [1] - 6880:19</p> <p>front [7] - 6877:25, 6901:9, 6902:9, 6904:6, 6904:9, 6917:16, 6944:24</p> <p>fruition [1] - 6894:10</p> <p>frustration [1] - 6847:10</p> <p>fuel [2] - 6783:2, 6887:18</p> <p>full [7] - 6777:2, 6871:25, 6873:14, 6914:16, 6915:14, 6931:9, 6965:18</p> <p>functioning [3] - 6784:2, 6784:5, 6951:19</p> <p>fund [1] - 6889:15</p> <p>Funda [5] - 6780:18, 6781:16, 6785:7, 6815:11, 6862:4</p> <p>funda's [1] - 6958:14</p> <p>fundamental [2] - 6791:19, 6842:9</p> <p>fundamentally [2] - 6817:17, 6878:13</p> <p>funding [5] - 6887:18, 6889:14, 6889:21, 6905:1, 6945:13</p> <p>funds [1] - 6945:13</p> <p>future [9] - 6779:9, 6784:18, 6787:23, 6792:25, 6793:23, 6794:13, 6884:24, 6905:14, 6907:17</p>	<p>6914:11, 6920:1, 6945:8</p> <p>General [3] - 6867:6, 6883:18, 6886:18</p> <p>general-card [1] - 6914:11</p> <p>general-purpose [1] - 6914:11</p> <p>generally [2] - 6798:22, 6855:10</p> <p>generate [3] - 6812:2, 6815:23, 6887:18</p> <p>Gentile [4] - 6774:23, 6775:23, 6862:17, 6862:18</p> <p>GENTILE [6] - 6773:9, 6774:23, 6775:25, 6776:3, 6862:18, 6966:25</p> <p>genuinely [1] - 6884:14</p> <p>George [1] - 6942:18</p> <p>Gibson [1] - 6793:11</p> <p>Gilbert [1] - 6806:21</p> <p>Gilbert's [2] - 6806:19, 6878:23</p> <p>Gilligan [13] - 6804:22, 6820:24, 6828:19, 6890:25, 6897:18, 6917:15, 6917:25, 6918:22, 6933:7, 6937:6, 6937:22, 6938:4, 6939:17</p> <p>given [7] - 6777:11, 6896:20, 6910:24, 6928:17, 6930:4, 6946:7, 6961:21</p> <p>glad [1] - 6778:3</p> <p>GLASS [3] - 6773:8, 6774:20, 6774:22</p> <p>Glass [1] - 6774:20</p> <p>glass [1] - 6774:21</p> <p>Glass's [1] - 6857:23</p> <p>glass's [1] - 6785:4</p> <p>Glenn [1] - 6828:20</p> <p>global [1] - 6840:4</p> <p>gloss [1] - 6853:24</p> <p>goal [4] - 6869:7, 6872:7, 6878:8, 6945:21</p> <p>gosh [1] - 6787:18</p> <p>Government [22] - 6777:11, 6924:5, 6925:9, 6928:1, 6929:9, 6929:25, 6930:16, 6930:21, 6930:22, 6931:18, 6931:23, 6931:24, 6932:1, 6932:5, 6932:13, 6933:4, 6934:7, 6935:22, 6938:8, 6941:22, 6942:6</p> <p>government [81] - 6808:3, 6866:13, 6866:17, 6866:25, 6867:3, 6867:10, 6867:15, 6868:13, 6869:2, 6869:6, 6869:14, 6869:21, 6870:14, 6870:17, 6871:11, 6873:16, 6874:1, 6874:18, 6875:1, 6875:17, 6876:22, 6878:11, 6878:13, 6878:19, 6879:17, 6881:9, 6881:15, 6882:2, 6882:7, 6882:13, 6883:8, 6883:15, 6884:1, 6884:14, 6885:15, 6887:7, 6887:15, 6887:19, 6887:22, 6888:10, 6889:4, 6889:17, 6890:15, 6890:21, 6891:14, 6893:16, 6894:14, 6894:20, 6896:1, 6896:12, 6898:6, 6898:9, 6898:23, 6899:4, 6902:12, 6906:9, 6906:12, 6907:20, 6908:17, 6909:10, 6910:1, 6911:6, 6911:11, 6912:23, 6913:8, 6914:10, 6914:18, 6915:20, 6916:15, 6916:17, 6919:9, 6919:13, 6920:21, 6944:22, 6945:19, 6945:23, 6947:10, 6966:22</p> <p>government's [19] - 6868:23, 6869:5, 6870:24, 6882:11, 6885:7, 6892:8,</p>
G		
<p>gain [5] - 6788:13, 6788:14, 6788:21, 6789:9, 6937:8</p> <p>gained [1] - 6779:4</p> <p>game [1] - 6936:10</p> <p>gap [3] - 6787:4, 6933:24</p> <p>GARAUFIS [3] - 6772:20, 6774:2, 6823:2</p> <p>GEICO [2] - 6936:11, 6936:18</p> <p>general [11] - 6782:5, 6794:6, 6809:2, 6828:3, 6853:11, 6853:12, 6854:18,</p>		

<p>6892:19, 6892:24, 6894:12, 6900:23, 6901:24, 6912:10, 6915:22, 6916:14, 6917:2, 6918:24, 6944:5, 6944:15, 6946:13</p> <p>Government's [5] - 6777:17, 6926:12, 6935:19, 6941:1, 6942:12</p> <p>grand [1] - 6954:7</p> <p>great [9] - 6819:20, 6821:25, 6822:2, 6822:22, 6878:16, 6885:6, 6887:9, 6903:3, 6929:22</p> <p>greater [1] - 6937:8</p> <p>green [3] - 6840:21, 6840:23, 6841:4</p> <p>Grocery [1] - 6913:5</p> <p>groom [1] - 6783:2</p> <p>gross [3] - 6880:8, 6880:10, 6926:19</p> <p>ground [1] - 6793:8</p> <p>group [7] - 6792:11, 6807:25, 6826:13, 6828:1, 6912:16, 6938:20, 6957:5</p> <p>groups [2] - 6807:25, 6893:24</p> <p>grow [1] - 6791:18</p> <p>growing [9] - 6798:22, 6799:1, 6799:4, 6799:5, 6918:5, 6921:6, 6921:8, 6921:9</p> <p>grows [1] - 6933:24</p> <p>growth [2] - 6918:8, 6918:9</p> <p>guarantee [5] - 6819:12, 6856:7, 6860:12, 6888:1, 6894:6</p> <p>guaranteed [1] - 6958:20</p> <p>guess [6] - 6796:1, 6838:6, 6850:6, 6858:2, 6890:2, 6961:14</p> <p>guesswork [1] - 6868:23</p> <p>GUNTHER [1] - 6773:20</p> <p>Gunther [1] - 6775:17</p> <p>Gutierrez [1] - 6942:17</p> <p>guy [15] - 6780:21, 6780:23, 6788:13, 6788:14, 6788:19, 6789:9, 6789:13, 6791:19, 6791:23, 6791:24, 6885:12, 6890:6, 6959:21, 6959:23, 6959:25</p> <p>guys [2] - 6885:10, 6937:19</p>	<p>6800:5, 6800:11, 6800:12, 6801:3, 6801:8, 6803:2, 6803:9, 6808:9, 6811:25, 6815:15, 6815:21, 6815:25, 6816:15, 6817:6, 6877:18, 6892:11, 6892:13, 6892:25, 6930:18, 6939:18, 6950:11, 6951:7, 6951:17, 6952:10, 6953:25</p> <p>harm's [1] - 6890:16</p> <p>harmed [4] - 6783:24, 6828:5, 6828:7, 6830:25</p> <p>harsh [4] - 6821:11, 6959:13, 6960:12, 6960:25</p> <p>Harvard [2] - 6886:7, 6886:8</p> <p>hat [1] - 6875:2</p> <p>Hawaii [1] - 6936:1</p> <p>head [1] - 6901:25</p> <p>Health [1] - 6912:16</p> <p>healthcare [1] - 6782:23</p> <p>hear [4] - 6866:8, 6871:13, 6872:18, 6886:20</p> <p>heard [38] - 6778:19, 6778:21, 6779:23, 6782:20, 6785:20, 6785:24, 6805:21, 6810:3, 6819:4, 6820:15, 6820:17, 6825:1, 6830:5, 6830:13, 6834:10, 6835:3, 6836:2, 6838:10, 6841:2, 6844:22, 6844:23, 6854:25, 6861:4, 6889:5, 6903:22, 6907:22, 6908:5, 6930:25, 6939:17, 6947:10, 6950:2, 6952:23, 6954:22, 6958:13, 6962:16, 6963:18, 6964:10, 6965:10</p> <p>hearing [4] - 6780:7, 6845:25, 6942:8, 6966:21</p> <p>heavily [1] - 6874:11</p> <p>held [3] - 6871:18, 6883:11, 6931:22</p> <p>help [5] - 6834:5, 6884:19, 6902:6, 6942:5, 6942:14</p> <p>helped [1] - 6834:16</p> <p>helpful [1] - 6834:7</p> <p>herring [4] - 6830:7, 6931:24, 6932:1, 6932:2</p> <p>high [21] - 6789:3, 6796:12, 6806:8, 6809:23, 6810:2, 6812:9, 6847:9, 6854:17, 6896:2, 6896:4, 6896:6, 6896:16, 6896:17, 6896:22, 6897:3, 6914:17, 6934:7, 6941:15, 6958:10</p> <p>high-price [1] - 6958:10</p> <p>higher [42] - 6786:14, 6789:23, 6801:10, 6803:3, 6807:2, 6812:1, 6812:8, 6812:17, 6812:19, 6816:16, 6816:17, 6816:24, 6817:3, 6819:17, 6820:8, 6828:5, 6829:5, 6829:14, 6839:11, 6844:15, 6851:8, 6854:16, 6854:21, 6863:15, 6863:17, 6876:8, 6876:16, 6887:25, 6896:24, 6897:4, 6897:6, 6897:14, 6897:16, 6900:20, 6900:24, 6900:25, 6916:17, 6934:9, 6934:10, 6951:20, 6951:21, 6953:15</p> <p>highest [2] - 6788:15, 6829:2</p> <p>highlight [1] - 6949:21</p> <p>highlighted [1] - 6905:12</p> <p>highly [1] - 6905:8</p>	<p>Hilton [3] - 6837:1, 6837:2</p> <p>Hilton's [1] - 6837:2</p> <p>himself [2] - 6890:4, 6910:9</p> <p>hindsight [3] - 6796:15, 6796:18, 6939:16</p> <p>historically [1] - 6797:7</p> <p>history [8] - 6889:3, 6890:12, 6906:7, 6927:8, 6948:6, 6948:9, 6958:1, 6960:24</p> <p>Hochschild [17] - 6781:1, 6785:24, 6786:13, 6786:19, 6786:21, 6787:23, 6789:12, 6790:25, 6793:7, 6820:4, 6861:5, 6883:22, 6884:25, 6897:19, 6908:5, 6908:14, 6952:19</p> <p>Hochschild's [1] - 6906:21</p> <p>hold [5] - 6809:5, 6829:15, 6850:22, 6927:2, 6948:7</p> <p>Holtey [1] - 6782:25</p> <p>home [3] - 6904:10, 6927:19, 6929:2</p> <p>Home [1] - 6782:22</p> <p>honest [1] - 6947:6</p> <p>honestly [2] - 6928:6, 6948:3</p> <p>Honor [153] - 6774:7, 6774:12, 6774:17, 6774:22, 6774:25, 6775:2, 6775:4, 6775:6, 6775:11, 6775:13, 6775:16, 6776:1, 6776:8, 6776:13, 6776:16, 6776:23, 6777:6, 6777:7, 6778:8, 6779:11, 6780:2, 6780:6, 6814:8, 6816:5, 6818:20, 6822:22, 6823:10, 6833:20, 6833:24, 6834:7, 6834:20, 6836:8, 6840:12, 6840:14, 6847:2, 6856:2, 6859:9, 6862:15, 6862:19, 6863:25, 6864:4, 6865:19, 6865:25, 6866:3, 6866:8, 6866:19, 6866:24, 6868:12, 6868:22, 6869:16, 6871:8, 6871:18, 6872:11, 6873:2, 6874:14, 6874:21, 6875:4, 6875:18, 6876:18, 6877:5, 6877:12, 6878:4, 6878:7, 6878:16, 6881:2, 6881:19, 6882:7, 6882:22, 6882:24, 6883:2, 6883:10, 6884:5, 6885:6, 6885:23, 6886:14, 6886:20, 6886:24, 6888:6, 6888:20, 6890:6, 6891:11, 6891:15, 6892:8, 6893:3, 6893:8, 6894:9, 6894:17, 6895:3, 6896:1, 6898:11, 6899:1, 6899:16, 6900:4, 6900:22, 6901:1, 6901:8, 6902:14, 6903:22, 6905:15, 6906:20, 6910:24, 6912:4, 6912:18, 6913:10, 6914:6, 6915:4, 6916:19, 6917:9, 6918:11, 6919:17, 6920:11, 6922:10, 6923:2, 6923:17, 6923:19, 6925:3, 6925:6, 6927:4, 6928:18, 6928:20, 6929:8, 6929:17, 6931:5, 6932:16, 6933:18, 6934:3, 6934:23, 6935:24, 6936:22, 6937:2, 6939:16, 6940:6, 6940:12, 6940:19, 6942:7, 6944:1, 6944:25, 6945:22, 6946:11, 6946:21, 6947:6, 6948:5, 6949:2, 6949:17, 6950:18, 6959:14, 6966:13, 6966:20, 6966:23, 6966:25, 6967:2</p> <p>Honor's [2] - 6778:1, 6872:2</p> <p>HONORABLE [1] - 6772:20</p>
H		
<p>half [9] - 6872:4, 6881:5, 6881:16, 6888:11, 6899:14, 6906:4, 6908:21, 6938:3, 6959:5</p> <p>Hall [1] - 6858:4</p> <p>HAMER [2] - 6773:5, 6774:11</p> <p>Hamer [1] - 6774:11</p> <p>hand [2] - 6853:10, 6865:20</p> <p>handed [1] - 6865:14</p> <p>handful [1] - 6941:6</p> <p>hands [1] - 6852:5</p> <p>hangs [1] - 6875:1</p> <p>happily [1] - 6933:19</p> <p>happy [3] - 6784:25, 6856:22, 6886:19</p> <p>hard [4] - 6789:13, 6801:20, 6909:7, 6960:21</p> <p>hardcopy [1] - 6777:1</p> <p>harder [4] - 6781:17, 6799:24, 6843:10, 6860:3</p> <p>harm [28] - 6784:1, 6787:7, 6787:9,</p>		

<p>hope [12] - 6776:8, 6776:9, 6779:24, 6785:4, 6797:16, 6823:10, 6848:17, 6862:14, 6867:17, 6867:22, 6906:9, 6945:25</p> <p>hopefully [1] - 6910:14</p> <p>hoping [1] - 6822:11</p> <p>horizontal [4] - 6874:6, 6874:8, 6874:9, 6875:17</p> <p>horrors [3] - 6946:24, 6947:4, 6947:15</p> <p>hostile [2] - 6937:20, 6944:20</p> <p>hostility [2] - 6937:22, 6938:2</p> <p>hotel [4] - 6835:18, 6836:4, 6927:16</p> <p>hour [1] - 6869:1</p> <p>hours [1] - 6775:19</p> <p>house [3] - 6910:4, 6921:7, 6921:10</p> <p>Houston [8] - 6830:17, 6830:20, 6832:1, 6832:7, 6842:22, 6965:15, 6965:17</p> <p>huge [11] - 6782:6, 6845:20, 6850:12, 6853:1, 6853:17, 6922:9, 6933:9, 6936:5, 6962:7, 6962:13, 6965:16</p> <p>hundred [3] - 6908:8, 6908:24, 6926:4</p> <p>hundreds [1] - 6831:13</p> <p>hungry [1] - 6927:23</p> <p>hurt [2] - 6905:4, 6909:11</p> <p>hurts [1] - 6808:10</p> <p>hypothetical [8] - 6824:24, 6825:6, 6825:9, 6825:18, 6825:20, 6914:3, 6916:1, 6963:10</p> <p>hypotheticals [1] - 6913:22</p>	<p>immediate [6] - 6814:17, 6814:20, 6837:21, 6863:4, 6883:12</p> <p>immediately [2] - 6842:23, 6883:21</p> <p>impact [5] - 6878:1, 6883:10, 6905:20, 6907:2, 6922:18</p> <p>impeded [5] - 6789:25, 6793:22, 6793:23, 6794:18, 6952:6</p> <p>impeding [1] - 6792:24</p> <p>impending [1] - 6790:3</p> <p>impermeable [1] - 6881:3</p> <p>implement [1] - 6908:18</p> <p>implemented [3] - 6841:10, 6888:8, 6907:19</p> <p>implementing [1] - 6824:23</p> <p>implication [2] - 6852:16, 6940:14</p> <p>implications [1] - 6831:11</p> <p>implicit [1] - 6820:3</p> <p>implicitly [2] - 6791:9, 6843:21</p> <p>importance [1] - 6860:16</p> <p>important [26] - 6780:22, 6783:15, 6785:19, 6791:1, 6791:4, 6796:4, 6796:16, 6809:24, 6818:25, 6823:23, 6827:9, 6849:13, 6852:19, 6857:4, 6863:23, 6866:15, 6867:2, 6905:15, 6908:15, 6919:3, 6929:10, 6929:16, 6929:17, 6929:25, 6955:14, 6956:17</p> <p>importantly [3] - 6888:17, 6938:4, 6945:5</p> <p>impose [4] - 6810:19, 6854:23, 6858:25, 6961:25</p> <p>imposed [5] - 6812:17, 6828:5, 6840:15, 6863:11, 6946:25</p> <p>impossible [2] - 6937:18, 6957:10</p> <p>impressive [1] - 6960:19</p> <p>improving [1] - 6903:17</p> <p>IN [1] - 6772:15</p> <p>in-house [1] - 6910:4</p> <p>inactive [2] - 6933:13, 6933:14</p> <p>inappropriate [1] - 6950:6</p> <p>inasmuch [1] - 6833:11</p> <p>INC [2] - 6772:11, 6772:12</p> <p>incentive [5] - 6780:18, 6788:1, 6794:9, 6923:9, 6950:14</p> <p>incentives [4] - 6781:21, 6848:22, 6862:8, 6958:15</p> <p>include [1] - 6966:6</p> <p>included [2] - 6795:11, 6966:7</p> <p>includes [1] - 6845:14</p> <p>including [8] - 6778:20, 6790:15, 6795:10, 6812:9, 6815:7, 6823:15, 6831:10, 6871:24</p> <p>income [2] - 6817:25, 6850:14</p> <p>Income [2] - 6840:17, 6850:11</p> <p>inconsistent [5] - 6888:15, 6890:22, 6917:4, 6933:20, 6934:1</p> <p>inconvenience [5] - 6846:17, 6909:23, 6909:24, 6910:10, 6911:1</p> <p>INCORPORATED [1] - 6772:12</p> <p>incorrect [2] - 6815:19, 6868:11</p> <p>incorrectly [1] - 6817:2</p> <p>increase [37] - 6781:21, 6785:13,</p>	<p>6785:14, 6785:17, 6786:16, 6801:10, 6812:5, 6815:9, 6820:7, 6824:18, 6824:20, 6825:22, 6828:3, 6842:1, 6844:5, 6844:9, 6844:10, 6844:13, 6844:17, 6845:3, 6845:4, 6845:13, 6846:3, 6847:11, 6850:4, 6850:25, 6851:20, 6855:3, 6862:8, 6862:9, 6899:9, 6937:24, 6950:25, 6952:8, 6953:16, 6963:10, 6963:11</p> <p>increased [10] - 6785:22, 6787:3, 6787:8, 6789:1, 6840:16, 6894:21, 6911:21, 6924:21, 6952:17, 6953:25</p> <p>increases [20] - 6793:16, 6826:1, 6835:24, 6839:13, 6840:16, 6840:18, 6840:20, 6840:21, 6840:23, 6841:3, 6841:5, 6841:8, 6841:10, 6844:7, 6844:23, 6854:23, 6855:1, 6880:14, 6939:1</p> <p>increasing [4] - 6787:18, 6800:6, 6851:11, 6951:9</p> <p>incredible [2] - 6852:9, 6853:8</p> <p>incredibly [2] - 6871:12, 6912:10</p> <p>incremental [1] - 6788:1</p> <p>incur [1] - 6951:22</p> <p>incurred [1] - 6863:13</p> <p>indeed [5] - 6847:10, 6867:9, 6869:17, 6882:15, 6884:25</p> <p>independent [3] - 6796:7, 6811:2, 6936:16</p> <p>Indiana [10] - 6783:25, 6800:24, 6801:1, 6801:6, 6874:10, 6875:3, 6876:19, 6951:11, 6951:23, 6951:25</p> <p>indicated [1] - 6856:14</p> <p>indication [1] - 6955:21</p> <p>individual [4] - 6836:25, 6916:4, 6929:21, 6938:20</p> <p>individuals [1] - 6832:5</p> <p>industries [8] - 6803:16, 6830:16, 6854:25, 6855:8, 6855:9, 6925:19, 6925:20, 6926:12</p> <p>Industries [2] - 6828:21, 6829:6</p> <p>industry [28] - 6784:20, 6804:18, 6804:23, 6808:15, 6810:20, 6816:10, 6828:22, 6828:24, 6829:2, 6831:1, 6831:2, 6831:18, 6831:22, 6847:5, 6847:7, 6854:4, 6855:4, 6897:20, 6906:10, 6925:24, 6925:25, 6926:8, 6964:12, 6965:13, 6965:14, 6965:18, 6965:20</p> <p>industry-specific [1] - 6828:22</p> <p>industry-variable [1] - 6829:2</p> <p>inexorable [2] - 6817:18, 6820:2</p> <p>inexplicably [1] - 6888:14</p> <p>inference [1] - 6885:7</p> <p>inflated [1] - 6863:20</p> <p>inflicted [1] - 6933:7</p> <p>influence [2] - 6904:2, 6904:11</p> <p>information [4] - 6794:2, 6858:17, 6863:1, 6876:9</p> <p>inherently [1] - 6858:10</p> <p>initial [1] - 6777:18</p>
I		
<p>IBM [1] - 6932:20</p> <p>idea [20] - 6784:21, 6792:19, 6798:17, 6811:4, 6815:22, 6817:17, 6819:1, 6821:1, 6847:17, 6853:6, 6880:17, 6888:13, 6909:13, 6921:16, 6922:4, 6933:25, 6938:17, 6938:18, 6940:7, 6947:11</p> <p>ideas [1] - 6795:10</p> <p>identifying [1] - 6831:10</p> <p>ignore [7] - 6807:15, 6840:23, 6879:19, 6881:5, 6881:16, 6963:20, 6963:23</p> <p>ignored [3] - 6851:6, 6866:15, 6908:25</p> <p>ignores [1] - 6866:13</p> <p>ignoring [2] - 6881:17, 6895:10</p> <p>IHAN [1] - 6773:6</p> <p>Ihan [1] - 6774:14</p> <p>II [1] - 6772:16</p> <p>III [1] - 6773:2</p> <p>IKEA [3] - 6856:24, 6885:11, 6885:12</p> <p>Ikea [3] - 6784:15, 6909:15</p> <p>illegal [2] - 6864:2, 6897:7</p> <p>illuminate [1] - 6965:3</p> <p>illustrated [2] - 6785:5, 6842:14</p> <p>illustrates [1] - 6915:22</p> <p>illustration [1] - 6918:11</p> <p>Image [1] - 6785:16</p> <p>imagination [1] - 6847:5</p> <p>imagine [2] - 6808:3, 6808:4</p> <p>imaging [2] - 6801:14, 6900:10</p>	<p>impose [4] - 6810:19, 6854:23, 6858:25, 6961:25</p> <p>imposed [5] - 6812:17, 6828:5, 6840:15, 6863:11, 6946:25</p> <p>impossible [2] - 6937:18, 6957:10</p> <p>impressive [1] - 6960:19</p> <p>improving [1] - 6903:17</p> <p>IN [1] - 6772:15</p> <p>in-house [1] - 6910:4</p> <p>inactive [2] - 6933:13, 6933:14</p> <p>inappropriate [1] - 6950:6</p> <p>inasmuch [1] - 6833:11</p> <p>INC [2] - 6772:11, 6772:12</p> <p>incentive [5] - 6780:18, 6788:1, 6794:9, 6923:9, 6950:14</p> <p>incentives [4] - 6781:21, 6848:22, 6862:8, 6958:15</p> <p>include [1] - 6966:6</p> <p>included [2] - 6795:11, 6966:7</p> <p>includes [1] - 6845:14</p> <p>including [8] - 6778:20, 6790:15, 6795:10, 6812:9, 6815:7, 6823:15, 6831:10, 6871:24</p> <p>income [2] - 6817:25, 6850:14</p> <p>Income [2] - 6840:17, 6850:11</p> <p>inconsistent [5] - 6888:15, 6890:22, 6917:4, 6933:20, 6934:1</p> <p>inconvenience [5] - 6846:17, 6909:23, 6909:24, 6910:10, 6911:1</p> <p>INCORPORATED [1] - 6772:12</p> <p>incorrect [2] - 6815:19, 6868:11</p> <p>incorrectly [1] - 6817:2</p> <p>increase [37] - 6781:21, 6785:13,</p>	<p>6785:14, 6785:17, 6786:16, 6801:10, 6812:5, 6815:9, 6820:7, 6824:18, 6824:20, 6825:22, 6828:3, 6842:1, 6844:5, 6844:9, 6844:10, 6844:13, 6844:17, 6845:3, 6845:4, 6845:13, 6846:3, 6847:11, 6850:4, 6850:25, 6851:20, 6855:3, 6862:8, 6862:9, 6899:9, 6937:24, 6950:25, 6952:8, 6953:16, 6963:10, 6963:11</p> <p>increased [10] - 6785:22, 6787:3, 6787:8, 6789:1, 6840:16, 6894:21, 6911:21, 6924:21, 6952:17, 6953:25</p> <p>increases [20] - 6793:16, 6826:1, 6835:24, 6839:13, 6840:16, 6840:18, 6840:20, 6840:21, 6840:23, 6841:3, 6841:5, 6841:8, 6841:10, 6844:7, 6844:23, 6854:23, 6855:1, 6880:14, 6939:1</p> <p>increasing [4] - 6787:18, 6800:6, 6851:11, 6951:9</p> <p>incredible [2] - 6852:9, 6853:8</p> <p>incredibly [2] - 6871:12, 6912:10</p> <p>incremental [1] - 6788:1</p> <p>incur [1] - 6951:22</p> <p>incurred [1] - 6863:13</p> <p>indeed [5] - 6847:10, 6867:9, 6869:17, 6882:15, 6884:25</p> <p>independent [3] - 6796:7, 6811:2, 6936:16</p> <p>Indiana [10] - 6783:25, 6800:24, 6801:1, 6801:6, 6874:10, 6875:3, 6876:19, 6951:11, 6951:23, 6951:25</p> <p>indicated [1] - 6856:14</p> <p>indication [1] - 6955:21</p> <p>individual [4] - 6836:25, 6916:4, 6929:21, 6938:20</p> <p>individuals [1] - 6832:5</p> <p>industries [8] - 6803:16, 6830:16, 6854:25, 6855:8, 6855:9, 6925:19, 6925:20, 6926:12</p> <p>Industries [2] - 6828:21, 6829:6</p> <p>industry [28] - 6784:20, 6804:18, 6804:23, 6808:15, 6810:20, 6816:10, 6828:22, 6828:24, 6829:2, 6831:1, 6831:2, 6831:18, 6831:22, 6847:5, 6847:7, 6854:4, 6855:4, 6897:20, 6906:10, 6925:24, 6925:25, 6926:8, 6964:12, 6965:13, 6965:14, 6965:18, 6965:20</p> <p>industry-specific [1] - 6828:22</p> <p>industry-variable [1] - 6829:2</p> <p>inexorable [2] - 6817:18, 6820:2</p> <p>inexplicably [1] - 6888:14</p> <p>inference [1] - 6885:7</p> <p>inflated [1] - 6863:20</p> <p>inflicted [1] - 6933:7</p> <p>influence [2] - 6904:2, 6904:11</p> <p>information [4] - 6794:2, 6858:17, 6863:1, 6876:9</p> <p>inherently [1] - 6858:10</p> <p>initial [1] - 6777:18</p>

<p>initiated [1] - 6796:11</p> <p>initiative [1] - 6961:11</p> <p>injunction [2] - 6944:23, 6948:8</p> <p>injured [4] - 6808:5, 6808:8, 6881:7</p> <p>injures [1] - 6945:10</p> <p>inkling [1] - 6901:25</p> <p>innovate [2] - 6792:12, 6794:9</p> <p>innovating [1] - 6794:7</p> <p>innovation [13] - 6791:21, 6791:22, 6792:1, 6792:24, 6793:3, 6794:4, 6794:5, 6794:10, 6794:16, 6800:11, 6801:17, 6877:21</p> <p>innovative [4] - 6791:24, 6793:15, 6860:25, 6861:2</p> <p>input [1] - 6808:17</p> <p>inquired [1] - 6778:4</p> <p>insight [1] - 6799:12</p> <p>insights [1] - 6779:4</p> <p>insistence [18] - 6839:2, 6839:22, 6854:17, 6854:19, 6854:20, 6909:25, 6910:2, 6935:15, 6936:11, 6936:15, 6940:14, 6940:15, 6940:20, 6940:21, 6941:10, 6941:12, 6941:17, 6945:12</p> <p>insistent [5] - 6832:16, 6835:17, 6839:4, 6940:18</p> <p>insisting [4] - 6804:12, 6922:12, 6922:14, 6923:5</p> <p>instance [2] - 6847:25, 6874:24</p> <p>instead [10] - 6777:23, 6792:7, 6825:14, 6836:1, 6851:5, 6872:17, 6879:9, 6908:23, 6945:20, 6963:4</p> <p>insufficient [1] - 6922:4</p> <p>insulate [1] - 6902:13</p> <p>insulated [2] - 6787:20, 6863:19</p> <p>insurance [1] - 6952:1</p> <p>intention [1] - 6778:3</p> <p>interaction [1] - 6834:18</p> <p>interbrand [2] - 6783:16, 6783:18</p> <p>interchangeability [6] - 6804:14, 6824:7, 6824:9, 6824:24, 6825:18, 6916:3</p> <p>interchangeable [10] - 6804:13, 6806:6, 6806:9, 6807:2, 6807:17, 6824:14, 6879:4, 6879:10, 6879:13, 6915:20</p> <p>interdependent [1] - 6803:23</p> <p>interest [12] - 6780:3, 6817:25, 6818:13, 6827:2, 6843:12, 6857:11, 6880:23, 6880:25, 6901:6, 6914:16, 6950:14, 6960:5</p> <p>interested [3] - 6777:13, 6786:10, 6834:1</p> <p>interesting [2] - 6836:5, 6860:18</p> <p>interfere [1] - 6856:18</p> <p>interference [1] - 6952:2</p> <p>intermediaries [2] - 6933:23, 6945:3</p> <p>internal [7] - 6787:2, 6828:18, 6835:4, 6905:9, 6921:21, 6923:20, 6946:1</p> <p>internally [3] - 6795:15, 6839:3, 6918:13</p> <p>INTERNATIONAL [1] - 6772:11</p> <p>international [2] - 6840:22, 6926:3</p>	<p>Internet [1] - 6902:21</p> <p>interpretation [2] - 6817:8, 6822:14</p> <p>interrupt [1] - 6778:22</p> <p>interstate [1] - 6926:2</p> <p>intervention [3] - 6790:6, 6790:7, 6790:17</p> <p>intra [1] - 6873:22</p> <p>introduce [1] - 6798:6</p> <p>invest [1] - 6898:20</p> <p>investing [1] - 6940:20</p> <p>investment [4] - 6911:24, 6935:8, 6935:12, 6941:13</p> <p>investments [3] - 6902:5, 6902:9, 6902:10</p> <p>investors [2] - 6935:7, 6935:12</p> <p>involve [1] - 6808:22</p> <p>involved [3] - 6818:6, 6818:20, 6931:4</p> <p>involves [3] - 6899:12, 6951:7, 6953:15</p> <p>involving [4] - 6792:13, 6899:5, 6922:2</p> <p>IOWA [1] - 6772:4</p> <p>Isolated [1] - 6875:23</p> <p>issuance [1] - 6807:10</p> <p>issue [22] - 6794:18, 6797:9, 6801:12, 6806:13, 6806:20, 6807:18, 6809:9, 6809:25, 6834:16, 6869:4, 6886:11, 6899:3, 6903:9, 6903:10, 6922:12, 6922:14, 6926:13, 6932:11, 6940:12, 6942:9, 6950:3, 6961:5</p> <p>issuer [10] - 6804:25, 6805:13, 6805:15, 6805:17, 6820:1, 6950:1, 6950:15, 6955:1, 6963:3</p> <p>issuers [19] - 6805:8, 6805:9, 6805:20, 6805:25, 6806:2, 6806:4, 6806:11, 6806:12, 6807:13, 6808:16, 6815:7, 6815:15, 6819:14, 6833:10, 6834:24, 6950:3, 6950:12, 6950:19, 6950:24</p> <p>issues [8] - 6782:17, 6804:1, 6804:7, 6823:6, 6823:13, 6912:7, 6912:20, 6949:20</p> <p>issuing [11] - 6834:12, 6852:4, 6867:22, 6955:3, 6955:4, 6955:6, 6955:13, 6955:19, 6955:24, 6956:20, 6963:1</p> <p>issuing-side [1] - 6852:4</p> <p>itself [17] - 6783:24, 6805:17, 6805:18, 6807:8, 6830:6, 6830:9, 6830:19, 6843:7, 6857:10, 6858:3, 6877:11, 6907:10, 6916:15, 6952:18, 6960:15, 6961:1, 6963:14</p>	<p>6831:20, 6903:16</p> <p>JOHN [1] - 6773:5</p> <p>John [2] - 6784:14, 6856:24</p> <p>join [1] - 6786:23</p> <p>joined [1] - 6863:23</p> <p>joint [2] - 6796:6, 6886:19</p> <p>jointly [1] - 6932:3</p> <p>Jones [1] - 6867:10</p> <p>Journal [1] - 6883:14</p> <p>Judge [11] - 6772:20, 6774:2, 6823:2, 6867:10, 6876:4, 6876:14, 6932:19, 6948:13, 6948:18, 6948:19, 6948:24</p> <p>judge [4] - 6818:11, 6839:6, 6886:6, 6948:19</p> <p>judgment [5] - 6872:2, 6912:18, 6929:19, 6935:10, 6946:12</p> <p>judgments [1] - 6909:2</p> <p>jump [1] - 6903:17</p> <p>Justice [6] - 6773:2, 6831:10, 6868:17, 6885:17, 6886:1, 6954:17</p> <p>justification [2] - 6859:4, 6860:6</p> <p>justifications [1] - 6802:22</p> <p>justify [1] - 6820:8</p>
K		
<p>Katz [50] - 6787:16, 6803:13, 6816:22, 6824:25, 6825:9, 6826:4, 6827:21, 6827:24, 6828:6, 6842:3, 6843:6, 6844:12, 6852:15, 6853:15, 6869:4, 6869:23, 6881:21, 6881:22, 6882:18, 6884:6, 6887:8, 6887:20, 6892:1, 6905:18, 6913:2, 6914:2, 6915:25, 6924:6, 6924:17, 6925:15, 6925:21, 6926:9, 6926:16, 6930:8, 6935:16, 6938:13, 6941:25, 6944:6, 6945:14, 6952:23, 6952:24, 6953:5, 6953:19, 6962:9, 6963:15, 6963:19, 6964:13, 6964:15, 6964:21</p> <p>Katz's [7] - 6844:4, 6871:25, 6872:19, 6894:21, 6905:19, 6924:24, 6962:12</p> <p>keep [13] - 6775:21, 6783:15, 6784:25, 6799:24, 6819:20, 6863:6, 6890:7, 6891:12, 6901:19, 6912:24, 6913:14, 6936:21, 6965:1</p> <p>keeps [1] - 6856:22</p> <p>KEVIN [1] - 6773:13</p> <p>Kevin [1] - 6775:3</p> <p>key [1] - 6783:14</p> <p>kill [5] - 6889:21, 6890:11, 6893:15, 6905:1, 6935:11</p> <p>killed [2] - 6938:5, 6939:18</p> <p>KIM [2] - 6773:6, 6774:14</p> <p>Kim [1] - 6774:14</p> <p>Kimmet [1] - 6782:22</p> <p>kind [48] - 6790:6, 6791:7, 6792:24, 6797:23, 6799:19, 6801:13, 6803:17, 6805:15, 6808:23, 6809:20, 6810:9, 6810:11, 6810:13, 6811:12, 6812:12, 6817:16, 6817:18, 6834:17, 6834:19, 6834:25, 6835:21, 6837:9, 6837:22, 6837:23, 6838:2, 6838:21, 6839:20,</p>		
J		
<p>Jack [1] - 6780:18</p> <p>jackets [2] - 6879:9, 6879:16</p> <p>Jefferson [1] - 6876:3</p> <p>jeopardy [1] - 6905:2</p> <p>Jersey [1] - 6904:19</p> <p>JESSE [1] - 6773:19</p> <p>Jesse [1] - 6775:10</p> <p>Jet [1] - 6853:16</p> <p>JetBlue [1] - 6851:24</p> <p>job [5] - 6799:9, 6819:21, 6821:6,</p>		

<p>6849:25, 6850:1, 6859:19, 6859:24, 6902:13, 6904:5, 6907:10, 6918:19, 6923:2, 6924:21, 6925:11, 6935:13, 6936:6, 6941:10, 6944:20, 6945:2, 6945:9, 6952:5, 6963:4, 6965:20</p> <p>kinds [2] - 6794:19, 6909:2</p> <p>King [3] - 6927:25, 6928:6, 6928:8</p> <p>KMB [7] - 6801:14, 6875:20, 6882:22, 6899:20, 6899:22, 6900:9, 6912:15</p> <p>known [2] - 6830:10, 6939:19</p> <p>knows [6] - 6779:11, 6786:4, 6791:15, 6796:3, 6961:17, 6966:3</p> <p>Kodak [1] - 6785:16</p> <p>Korologos [1] - 6775:9</p> <p>KOROLOGOS [2] - 6773:18, 6775:8</p> <p>Kotelly [2] - 6948:19</p>	<p>least [5] - 6801:8, 6826:1, 6881:13, 6920:4, 6925:10</p> <p>leave [3] - 6868:10, 6927:15, 6935:8</p> <p>leaves [1] - 6940:12</p> <p>leaving [2] - 6818:2, 6866:23</p> <p>left [10] - 6853:10, 6856:4, 6859:9, 6894:2, 6908:3, 6927:18, 6929:2, 6942:25, 6959:11, 6963:17</p> <p>left-hand [1] - 6853:10</p> <p>legal [11] - 6783:14, 6785:19, 6800:22, 6807:21, 6824:10, 6869:8, 6871:1, 6874:23, 6878:8, 6945:20, 6955:24</p> <p>legally [2] - 6782:8, 6951:14</p> <p>legion [1] - 6911:14</p> <p>legislative [1] - 6961:23</p> <p>legitimate [2] - 6838:12, 6859:4</p> <p>lens [1] - 6924:15</p> <p>less [18] - 6788:10, 6799:1, 6815:8, 6842:17, 6843:9, 6843:13, 6843:23, 6843:24, 6851:7, 6873:11, 6894:16, 6894:17, 6894:18, 6910:8, 6932:17, 6955:23, 6959:16</p> <p>lesser [1] - 6939:23</p> <p>letters [1] - 6936:12</p> <p>letting [2] - 6810:22, 6845:9</p> <p>level [11] - 6786:24, 6788:5, 6789:21, 6809:23, 6810:2, 6934:8, 6941:15, 6950:15, 6950:17, 6957:13, 6958:19</p> <p>levels [2] - 6833:17, 6904:19</p> <p>leverage [2] - 6942:9, 6942:11</p> <p>Lexington [1] - 6773:16</p> <p>liability [7] - 6886:20, 6947:17, 6947:21, 6947:23, 6948:4, 6948:16, 6966:10</p> <p>lid [1] - 6888:11</p> <p>lies [4] - 6917:9, 6917:10, 6917:12</p> <p>life [1] - 6907:11</p> <p>life-threatening [1] - 6907:11</p> <p>light [3] - 6794:12, 6805:15, 6875:15</p> <p>likelihood [4] - 6794:13, 6907:3, 6910:13</p> <p>likely [5] - 6874:13, 6920:5, 6951:18, 6952:5, 6955:23</p> <p>limitation [1] - 6944:10</p> <p>limitations [1] - 6961:13</p> <p>limited [1] - 6801:6</p> <p>limiting [1] - 6862:23</p> <p>line [7] - 6816:25, 6853:5, 6853:15, 6853:17, 6853:19, 6858:1, 6952:14</p> <p>lines [1] - 6805:7</p> <p>linger [1] - 6911:18</p> <p>lingering [1] - 6903:4</p> <p>link [1] - 6800:6</p> <p>linked [1] - 6888:14</p> <p>lip [1] - 6878:12</p> <p>list [3] - 6792:1, 6795:10, 6961:7</p> <p>lists [2] - 6829:23, 6829:25</p> <p>literally [2] - 6871:25, 6922:9</p> <p>literature [3] - 6905:21, 6934:14, 6965:21</p> <p>litigation [4] - 6863:24, 6864:6, 6902:2, 6925:8</p>	<p>LITIGATION [2] - 6772:16, 6773:2</p> <p>litigation-driven [1] - 6925:8</p> <p>litmus [1] - 6804:14</p> <p>littered [1] - 6960:24</p> <p>lived [7] - 6842:21, 6889:3, 6890:12, 6901:22, 6906:7, 6906:20, 6945:18</p> <p>LLP [2] - 6773:11, 6773:15</p> <p>loan [2] - 6942:24, 6942:25</p> <p>lobby [1] - 6858:7</p> <p>local [1] - 6797:3</p> <p>location [1] - 6903:11</p> <p>locations [8] - 6872:21, 6883:5, 6884:23, 6892:10, 6908:12, 6931:7, 6933:6, 6941:2</p> <p>lodging [1] - 6829:11</p> <p>logic [6] - 6810:6, 6817:9, 6817:15, 6825:8, 6826:12, 6964:22</p> <p>logically [1] - 6847:18</p> <p>logistics [1] - 6777:7</p> <p>long-existing [1] - 6899:17</p> <p>Look [1] - 6850:25</p> <p>look [98] - 6788:20, 6791:15, 6792:15, 6796:17, 6798:20, 6801:4, 6801:6, 6802:17, 6803:20, 6804:20, 6805:12, 6805:24, 6808:16, 6820:12, 6822:15, 6823:11, 6824:12, 6826:12, 6828:4, 6828:16, 6828:17, 6829:8, 6829:15, 6840:2, 6843:19, 6844:13, 6850:17, 6851:15, 6851:22, 6854:20, 6856:21, 6858:18, 6866:11, 6868:7, 6869:20, 6870:13, 6870:22, 6874:1, 6874:5, 6874:12, 6874:16, 6874:17, 6874:22, 6874:25, 6875:4, 6875:7, 6877:2, 6879:21, 6881:5, 6881:21, 6882:9, 6887:2, 6887:7, 6888:16, 6888:17, 6888:21, 6893:25, 6895:1, 6895:12, 6897:24, 6898:7, 6899:14, 6899:19, 6900:2, 6903:24, 6905:14, 6905:18, 6906:21, 6907:18, 6908:15, 6909:5, 6909:6, 6914:1, 6916:5, 6918:1, 6918:20, 6918:23, 6925:16, 6925:17, 6926:10, 6926:16, 6926:25, 6929:13, 6930:6, 6934:19, 6936:12, 6937:22, 6950:3, 6952:4, 6956:17, 6958:1, 6961:2, 6962:23, 6964:17, 6965:4</p> <p>looked [12] - 6801:12, 6822:6, 6842:3, 6842:7, 6842:14, 6842:20, 6844:12, 6855:6, 6870:12, 6908:8, 6908:24, 6937:14</p> <p>looking [22] - 6790:7, 6792:12, 6796:14, 6796:17, 6801:8, 6801:25, 6804:17, 6829:12, 6844:1, 6856:14, 6874:18, 6881:17, 6882:8, 6905:19, 6906:15, 6916:4, 6921:19, 6930:12, 6934:6, 6953:4, 6958:22, 6964:22</p> <p>looks [5] - 6801:25, 6865:23, 6875:4, 6923:19, 6940:10</p> <p>loop [2] - 6806:22, 6820:1</p> <p>lose [7] - 6802:5, 6826:15, 6842:23, 6844:18, 6890:11, 6910:5, 6963:25</p> <p>loses [1] - 6955:22</p>
L		
<p>laboratory [1] - 6923:3</p> <p>lack [1] - 6932:18</p> <p>laid [2] - 6838:19, 6889:20</p> <p>language [3] - 6874:17, 6878:1, 6907:13</p> <p>lapped [1] - 6898:21</p> <p>large [2] - 6839:16, 6866:13</p> <p>largely [2] - 6866:11, 6866:13</p> <p>largest [5] - 6782:21, 6829:25, 6851:18, 6955:1, 6955:12</p> <p>last [16] - 6853:24, 6870:4, 6872:22, 6873:13, 6878:3, 6883:8, 6890:19, 6908:20, 6911:13, 6917:14, 6923:15, 6930:20, 6931:2, 6946:20, 6966:1</p> <p>lastly [1] - 6923:17</p> <p>late [1] - 6865:23</p> <p>latest [1] - 6851:23</p> <p>law [35] - 6782:11, 6783:6, 6809:13, 6810:23, 6817:8, 6827:24, 6858:22, 6861:12, 6871:5, 6871:6, 6871:8, 6874:3, 6874:7, 6876:20, 6877:4, 6877:9, 6878:17, 6896:4, 6899:16, 6899:17, 6900:1, 6912:21, 6913:11, 6913:18, 6913:25, 6916:13, 6932:16, 6940:9, 6944:2, 6945:9, 6956:8, 6966:8</p> <p>laws [32] - 6783:16, 6783:20, 6789:16, 6789:20, 6808:14, 6810:15, 6810:21, 6811:6, 6815:21, 6819:3, 6819:9, 6819:10, 6820:18, 6824:8, 6858:21, 6859:12, 6859:13, 6859:15, 6861:10, 6861:22, 6862:12, 6863:22, 6930:11, 6936:7, 6945:6, 6953:10, 6953:11, 6956:15, 6960:12, 6960:16, 6960:22, 6961:22</p> <p>lawsuit [5] - 6867:11, 6867:25, 6868:13, 6884:18, 6942:13</p> <p>lead [3] - 6800:12, 6812:1, 6959:9</p> <p>leads [1] - 6853:14</p> <p>learn [1] - 6778:18</p> <p>learned [2] - 6780:6, 6879:6</p> <p>leased [3] - 6846:7, 6848:5, 6848:7</p> <p>leasing [1] - 6848:12</p>		

<p>losing [4] - 6787:18, 6839:13, 6854:23, 6904:18</p> <p>loss [1] - 6814:23</p> <p>lost [9] - 6799:2, 6799:3, 6839:16, 6839:17, 6882:19, 6889:22, 6905:5, 6910:8, 6912:3</p> <p>Lounge [1] - 6848:8</p> <p>lounge [5] - 6846:2, 6846:7, 6846:9, 6848:8, 6904:19</p> <p>lounges [5] - 6845:6, 6848:14, 6849:25, 6904:20, 6937:20</p> <p>love [1] - 6961:17</p> <p>low [24] - 6780:18, 6781:2, 6781:4, 6781:12, 6784:7, 6786:7, 6786:11, 6786:12, 6786:16, 6786:18, 6787:4, 6787:16, 6791:19, 6791:23, 6859:22, 6860:25, 6892:13, 6892:18, 6907:21, 6930:17, 6933:1, 6952:15, 6960:5, 6960:6</p> <p>lower [25] - 6780:14, 6786:1, 6786:8, 6787:11, 6788:19, 6793:7, 6793:16, 6793:17, 6804:25, 6814:11, 6819:15, 6853:11, 6863:5, 6888:1, 6888:2, 6888:3, 6933:3, 6933:11, 6935:4, 6950:14, 6953:22, 6958:11, 6958:16, 6959:3, 6960:10</p> <p>lowered [1] - 6936:15</p> <p>lowering [1] - 6787:25</p> <p>loyal [1] - 6956:21</p> <p>loyalty [6] - 6919:18, 6920:16, 6920:25, 6935:15, 6941:14, 6945:15</p> <p>lumped [2] - 6805:5, 6921:14</p> <p>lunch [5] - 6777:15, 6777:17, 6777:18, 6777:19, 6864:8</p> <p>luncheon [1] - 6864:11</p> <p>luxury [1] - 6963:22</p>	<p>6935:2</p> <p>MARK [3] - 6773:5, 6773:7, 6773:19</p> <p>mark [1] - 6774:11</p> <p>Mark [2] - 6774:16, 6775:12</p> <p>marked [1] - 6865:10</p> <p>market [292] - 6780:7, 6780:11, 6780:15, 6780:17, 6780:25, 6782:7, 6782:18, 6783:4, 6784:3, 6784:20, 6786:2, 6788:7, 6789:14, 6789:21, 6790:2, 6790:21, 6790:22, 6791:17, 6792:25, 6794:10, 6794:17, 6796:7, 6796:12, 6798:23, 6799:14, 6800:2, 6800:16, 6800:20, 6801:24, 6802:1, 6802:3, 6802:5, 6802:16, 6802:21, 6803:11, 6803:12, 6803:14, 6803:15, 6803:21, 6803:25, 6804:2, 6804:4, 6804:5, 6804:7, 6804:10, 6804:12, 6804:13, 6804:15, 6805:5, 6805:8, 6805:10, 6806:3, 6806:7, 6806:10, 6806:15, 6806:17, 6807:7, 6807:11, 6810:10, 6810:22, 6811:1, 6811:18, 6814:18, 6816:8, 6817:12, 6818:5, 6818:6, 6819:13, 6819:18, 6819:25, 6820:9, 6820:12, 6823:16, 6823:21, 6824:3, 6824:6, 6824:11, 6824:13, 6824:19, 6824:21, 6824:22, 6825:1, 6825:5, 6825:9, 6825:17, 6826:7, 6827:20, 6827:22, 6827:23, 6828:3, 6829:17, 6830:8, 6830:25, 6832:19, 6832:22, 6832:25, 6833:2, 6833:7, 6838:6, 6838:7, 6838:8, 6838:12, 6838:14, 6838:20, 6839:1, 6839:6, 6841:6, 6841:10, 6844:18, 6848:5, 6848:16, 6853:24, 6854:2, 6854:6, 6854:10, 6854:13, 6854:14, 6854:15, 6854:18, 6855:10, 6855:11, 6859:19, 6860:10, 6860:17, 6861:20, 6863:10, 6866:7, 6866:17, 6866:25, 6868:9, 6868:11, 6869:10, 6869:14, 6869:15, 6869:18, 6870:13, 6871:15, 6871:22, 6871:24, 6872:2, 6872:3, 6872:5, 6876:13, 6876:24, 6878:10, 6878:12, 6878:18, 6878:20, 6879:3, 6879:7, 6879:10, 6879:11, 6879:20, 6880:3, 6881:4, 6881:16, 6882:4, 6885:11, 6887:15, 6887:16, 6888:15, 6889:18, 6893:7, 6893:8, 6894:2, 6897:6, 6897:22, 6898:2, 6898:4, 6898:23, 6899:8, 6899:10, 6899:12, 6899:14, 6899:18, 6899:24, 6899:25, 6900:2, 6902:17, 6902:19, 6903:19, 6903:20, 6904:14, 6908:4, 6909:2, 6910:1, 6910:2, 6912:5, 6912:6, 6912:11, 6912:14, 6912:19, 6912:22, 6912:23, 6912:25, 6913:4, 6913:7, 6913:8, 6913:10, 6913:14, 6913:18, 6914:5, 6914:8, 6914:10, 6914:11, 6914:19, 6915:21, 6915:24, 6916:14, 6916:20, 6916:24, 6917:6, 6917:8, 6917:10, 6917:11, 6918:20, 6925:2, 6925:10, 6925:11, 6925:13, 6925:22, 6925:24, 6926:1, 6926:3, 6926:5, 6927:3, 6927:4,</p>	<p>6927:10, 6928:3, 6928:5, 6928:6, 6928:13, 6928:16, 6928:18, 6928:19, 6929:6, 6929:8, 6929:11, 6929:24, 6930:9, 6930:10, 6930:23, 6931:16, 6934:22, 6935:18, 6940:8, 6941:10, 6941:18, 6941:19, 6945:25, 6951:16, 6951:19, 6952:16, 6953:13, 6954:1, 6955:3, 6955:4, 6955:6, 6955:13, 6955:19, 6955:24, 6956:20, 6958:2, 6960:2, 6960:8, 6960:10, 6961:5, 6961:6, 6961:14, 6962:13, 6962:15, 6963:8, 6964:2, 6964:12, 6964:14, 6964:20, 6964:23, 6965:2, 6965:4, 6965:8, 6965:22, 6965:24</p> <p>market-wide [4] - 6780:25, 6800:16, 6899:24, 6900:2</p> <p>marketing [1] - 6911:17</p> <p>marketplace [18] - 6790:12, 6859:1, 6861:13, 6867:9, 6867:18, 6867:24, 6903:8, 6909:1, 6918:21, 6920:8, 6923:16, 6929:22, 6930:5, 6954:5, 6957:11, 6957:12, 6958:23, 6959:22</p> <p>marketplaces [1] - 6800:18</p> <p>markets [29] - 6785:25, 6797:3, 6803:23, 6803:24, 6805:2, 6805:4, 6805:5, 6806:6, 6807:5, 6807:9, 6825:3, 6830:12, 6830:15, 6830:20, 6830:22, 6831:23, 6832:24, 6833:5, 6848:9, 6853:11, 6853:12, 6875:14, 6899:5, 6904:15, 6926:8, 6926:22, 6926:23, 6961:18, 6964:16</p> <p>marking [1] - 6966:18</p> <p>MARYLAND [1] - 6772:5</p> <p>MasterCard [61] - 6779:12, 6786:25, 6788:6, 6788:16, 6790:14, 6791:6, 6795:18, 6796:2, 6796:4, 6796:5, 6796:13, 6797:22, 6799:2, 6799:4, 6807:10, 6821:19, 6837:5, 6854:1, 6854:5, 6867:18, 6868:6, 6879:14, 6883:6, 6885:16, 6887:5, 6888:11, 6891:17, 6892:3, 6892:25, 6893:3, 6893:13, 6893:20, 6898:1, 6898:10, 6908:8, 6909:5, 6910:15, 6910:17, 6910:22, 6920:6, 6931:4, 6931:13, 6931:18, 6931:20, 6932:3, 6932:4, 6932:5, 6932:24, 6940:25, 6941:9, 6941:20, 6941:24, 6941:25, 6945:24, 6946:1, 6947:11, 6954:7, 6956:24, 6959:11, 6959:15, 6959:19</p> <p>MASTERCARD [1] - 6772:11</p> <p>MasterCard's [1] - 6877:17</p> <p>MasterCards [1] - 6903:11</p> <p>matched [1] - 6898:18</p> <p>material [1] - 6777:2</p> <p>matter [19] - 6783:3, 6796:5, 6845:20, 6848:3, 6850:16, 6858:9, 6896:4, 6901:8, 6902:5, 6902:11, 6903:3, 6904:5, 6932:13, 6943:2, 6948:25, 6952:11, 6955:16</p> <p>matters [3] - 6783:4, 6902:8, 6930:17</p> <p>McDonald's [2] - 6927:24, 6927:25</p> <p>McMahon [1] - 6932:19</p>
M		
<p>Mac [1] - 6927:24</p> <p>made-for-litigation [1] - 6902:2</p> <p>mailbox [1] - 6955:21</p> <p>main [3] - 6783:5, 6800:21, 6805:25</p> <p>maintain [2] - 6957:15, 6958:12</p> <p>maintenance [2] - 6873:9, 6873:12</p> <p>major [4] - 6786:9, 6822:5, 6851:18, 6886:3</p> <p>majority [3] - 6919:21, 6919:23, 6951:25</p> <p>man [1] - 6866:21</p> <p>managed [1] - 6830:1</p> <p>management [1] - 6798:15</p> <p>Manhattan [1] - 6865:24</p> <p>manner [1] - 6950:14</p> <p>manufacturer [1] - 6873:10</p> <p>map [1] - 6940:17</p> <p>margin [8] - 6829:5, 6855:5, 6925:16, 6926:19, 6926:20, 6926:25, 6927:1, 6927:2</p> <p>marginal [1] - 6816:19</p> <p>margins [5] - 6829:10, 6926:17, 6935:1,</p>		

<p>MCX [2] - 6792:11, 6793:10</p> <p>mean [17] - 6779:11, 6781:1, 6782:7, 6785:12, 6817:10, 6848:21, 6858:13, 6858:14, 6858:15, 6860:12, 6871:12, 6886:5, 6947:12, 6948:23, 6956:14, 6957:3, 6958:25</p> <p>meaning [1] - 6790:13</p> <p>meaningful [1] - 6863:20</p> <p>meaningless [1] - 6909:10</p> <p>means [13] - 6781:2, 6781:12, 6781:20, 6806:22, 6862:7, 6863:15, 6878:13, 6884:15, 6904:5, 6910:22, 6916:8, 6920:23, 6926:22</p> <p>meant [2] - 6799:5, 6822:9</p> <p>measure [2] - 6934:13, 6934:15</p> <p>measured [1] - 6844:9</p> <p>meat [1] - 6937:3</p> <p>mechanical [1] - 6772:24</p> <p>mechanism [18] - 6780:13, 6781:14, 6784:3, 6784:6, 6787:3, 6796:13, 6808:10, 6872:11, 6873:1, 6873:7, 6873:11, 6873:18, 6874:18, 6877:3, 6878:6, 6900:18, 6951:19, 6952:3</p> <p>meet [7] - 6801:21, 6811:22, 6815:1, 6815:4, 6815:16, 6834:2, 6952:20</p> <p>meets [1] - 6838:9</p> <p>member [2] - 6920:3, 6950:11</p> <p>members [3] - 6845:7, 6846:14, 6905:13</p> <p>membership's [1] - 6845:8</p> <p>membrane [1] - 6881:4</p> <p>memo [1] - 6938:3</p> <p>memory [1] - 6948:10</p> <p>men's [1] - 6879:7</p> <p>mention [6] - 6796:1, 6817:25, 6818:21, 6869:2, 6933:2, 6940:13</p> <p>mentioned [10] - 6818:18, 6818:19, 6866:19, 6872:19, 6872:20, 6881:21, 6888:6, 6888:9, 6901:10, 6940:14</p> <p>mentions [1] - 6860:18</p> <p>merchant [105] - 6780:12, 6781:6, 6781:9, 6781:16, 6782:2, 6782:4, 6784:9, 6784:19, 6785:20, 6786:8, 6786:11, 6786:15, 6786:17, 6788:21, 6791:1, 6791:2, 6793:6, 6805:1, 6805:21, 6812:1, 6813:5, 6813:10, 6813:23, 6813:24, 6816:15, 6816:24, 6817:19, 6817:20, 6820:8, 6824:16, 6824:17, 6825:11, 6826:3, 6826:14, 6827:14, 6827:15, 6827:16, 6832:9, 6832:12, 6832:25, 6834:18, 6835:13, 6835:17, 6837:3, 6837:24, 6852:7, 6853:6, 6857:6, 6857:25, 6861:15, 6863:4, 6863:9, 6868:2, 6868:6, 6869:21, 6869:24, 6872:21, 6878:20, 6880:20, 6880:22, 6881:6, 6881:7, 6881:9, 6883:5, 6884:16, 6884:23, 6887:20, 6889:11, 6892:10, 6895:9, 6897:1, 6901:14, 6904:16, 6906:25, 6908:6, 6908:12, 6916:8, 6917:11, 6918:24, 6919:5, 6919:18, 6921:2,</p>	<p>6921:5, 6921:8, 6921:23, 6922:5, 6922:12, 6923:9, 6923:11, 6923:14, 6932:8, 6940:23, 6942:7, 6944:6, 6944:17, 6957:6, 6963:9, 6963:14, 6963:21</p> <p>Merchant [2] - 6829:3, 6829:12</p> <p>merchant's [2] - 6814:10, 6862:23</p> <p>merchant-friendly [1] - 6786:8</p> <p>merchant-owned [1] - 6793:6</p> <p>merchants [220] - 6778:19, 6781:3, 6781:10, 6781:11, 6781:18, 6781:22, 6782:19, 6782:20, 6784:12, 6784:17, 6785:11, 6786:3, 6787:24, 6788:1, 6788:24, 6791:2, 6791:25, 6792:12, 6792:20, 6793:6, 6794:1, 6794:8, 6794:24, 6795:2, 6795:14, 6797:6, 6799:22, 6800:13, 6803:2, 6803:3, 6804:10, 6805:13, 6805:22, 6805:25, 6806:5, 6806:14, 6806:23, 6807:2, 6807:16, 6808:4, 6808:11, 6808:19, 6810:10, 6811:2, 6812:6, 6812:18, 6815:5, 6815:22, 6815:25, 6816:1, 6816:20, 6817:3, 6817:13, 6819:13, 6819:16, 6820:5, 6824:16, 6824:19, 6825:17, 6825:21, 6826:5, 6826:9, 6826:11, 6827:1, 6827:3, 6827:4, 6827:15, 6827:19, 6827:22, 6827:23, 6828:12, 6828:13, 6830:1, 6831:3, 6831:5, 6831:13, 6831:14, 6831:17, 6832:3, 6832:14, 6835:10, 6835:11, 6835:22, 6836:17, 6836:18, 6838:3, 6838:9, 6839:4, 6839:10, 6839:13, 6839:15, 6839:16, 6839:17, 6842:2, 6844:18, 6844:21, 6844:22, 6847:11, 6851:8, 6854:14, 6854:18, 6854:21, 6856:7, 6856:20, 6856:24, 6857:15, 6859:23, 6860:25, 6861:18, 6861:19, 6862:9, 6863:2, 6863:7, 6863:12, 6863:14, 6872:20, 6878:24, 6879:22, 6880:4, 6880:16, 6880:17, 6880:23, 6880:24, 6883:19, 6884:4, 6884:12, 6884:13, 6884:17, 6884:18, 6884:21, 6885:2, 6885:8, 6885:14, 6885:21, 6887:4, 6887:17, 6890:19, 6891:15, 6891:16, 6892:16, 6893:14, 6893:15, 6894:13, 6894:15, 6895:7, 6897:15, 6899:5, 6902:23, 6904:9, 6904:10, 6904:17, 6906:2, 6906:18, 6907:14, 6909:13, 6911:18, 6916:15, 6916:24, 6919:22, 6920:24, 6921:1, 6921:12, 6921:16, 6921:18, 6922:3, 6923:4, 6923:5, 6925:23, 6925:24, 6928:1, 6931:1, 6931:7, 6931:9, 6933:13, 6933:15, 6933:23, 6933:25, 6935:5, 6935:23, 6936:22, 6937:5, 6937:9, 6938:6, 6939:2, 6939:7, 6939:9, 6939:10, 6939:13, 6941:1, 6941:7, 6941:22, 6942:1, 6942:3, 6942:10, 6942:16, 6943:2, 6944:9, 6950:5, 6952:6, 6958:9, 6958:10, 6958:11, 6958:16, 6959:4, 6960:3, 6963:9, 6963:10, 6963:11, 6963:18, 6964:6</p>	<p>merchants' [2] - 6786:14, 6897:16</p> <p>merely [1] - 6873:6</p> <p>merger [4] - 6833:2, 6833:3, 6882:1, 6882:2</p> <p>mergers [3] - 6831:9, 6831:11, 6832:20</p> <p>merits [5] - 6795:7, 6889:5, 6889:12, 6906:20, 6947:9</p> <p>message [2] - 6888:23, 6891:8</p> <p>messenger [1] - 6888:23</p> <p>met [3] - 6816:13, 6854:8, 6944:19</p> <p>method [1] - 6924:2</p> <p>metrics [4] - 6930:19, 6932:10, 6932:12, 6933:2</p> <p>MICHIGAN [1] - 6772:5</p> <p>microphone [2] - 6823:6</p> <p>Microsoft [1] - 6948:6</p> <p>middle [7] - 6777:14, 6805:12, 6805:24, 6818:10, 6829:1, 6853:17, 6881:4</p> <p>Midland [1] - 6965:18</p> <p>might [40] - 6782:9, 6785:8, 6786:23, 6790:20, 6794:17, 6802:12, 6810:13, 6811:10, 6813:10, 6814:11, 6814:16, 6814:21, 6815:7, 6815:9, 6820:25, 6821:14, 6833:17, 6836:24, 6837:24, 6837:25, 6846:20, 6855:2, 6865:22, 6873:25, 6885:13, 6885:16, 6886:21, 6888:2, 6890:11, 6891:12, 6900:9, 6928:9, 6929:2, 6929:3, 6944:6, 6944:8, 6946:25, 6953:14, 6958:24</p> <p>migrating [1] - 6924:2</p> <p>miles [9] - 6842:21, 6842:22, 6842:25, 6843:1, 6843:11, 6843:16, 6843:22, 6852:18, 6852:21</p> <p>Miles [5] - 6843:9, 6843:10, 6843:13, 6843:18, 6843:20</p> <p>million [16] - 6872:20, 6881:14, 6883:5, 6883:19, 6884:22, 6884:23, 6885:13, 6887:3, 6890:19, 6892:9, 6908:12, 6930:24, 6935:5, 6937:23, 6940:25, 6941:2</p> <p>million-plus [1] - 6908:12</p> <p>millions [2] - 6914:14, 6943:3</p> <p>mind [5] - 6783:15, 6901:5, 6938:18, 6948:21, 6965:2</p> <p>minds [1] - 6918:7</p> <p>minus [2] - 6828:23, 6926:10</p> <p>minute [3] - 6805:4, 6822:23, 6949:9</p> <p>minutes [7] - 6776:3, 6776:10, 6862:20, 6869:1, 6909:18, 6949:6, 6949:8</p> <p>mirror [1] - 6939:5</p> <p>mischaracterization [1] - 6880:1</p> <p>mischaracterize [1] - 6877:5</p> <p>misleading [1] - 6882:3</p> <p>missed [1] - 6851:11</p> <p>MISSOURI [1] - 6772:6</p> <p>misspoken [1] - 6900:10</p> <p>misstate [2] - 6910:17, 6942:16</p> <p>mistake [2] - 6842:9, 6886:23</p> <p>mistakes [1] - 6842:8</p> <p>Mitch [2] - 6774:23, 6862:18</p> <p>MITCHELL [1] - 6773:9</p>
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<p>Mitchell ^[1] - 6793:20</p> <p>mix ^[5] - 6851:6, 6851:12, 6853:19, 6868:7, 6897:19</p> <p>mix-adjusted ^[1] - 6897:19</p> <p>mixed ^[1] - 6934:10</p> <p>mobile ^[4] - 6792:4, 6792:7, 6792:14, 6793:12</p> <p>model ^[44] - 6790:4, 6790:14, 6790:15, 6809:1, 6810:19, 6812:12, 6815:17, 6817:22, 6819:11, 6822:1, 6822:4, 6822:19, 6859:11, 6860:9, 6860:10, 6860:16, 6860:17, 6860:19, 6860:21, 6860:22, 6860:23, 6860:24, 6861:2, 6861:16, 6861:21, 6862:1, 6867:1, 6867:8, 6867:20, 6868:17, 6881:18, 6889:10, 6894:6, 6905:2, 6906:8, 6916:11, 6924:14, 6935:14, 6954:6, 6960:14, 6960:17, 6960:23</p> <p>models ^[1] - 6861:13</p> <p>modus ^[1] - 6954:13</p> <p>moment ^[16] - 6778:22, 6782:13, 6793:13, 6857:12, 6868:15, 6869:7, 6869:14, 6869:20, 6877:6, 6914:6, 6917:14, 6922:7, 6925:17, 6940:15, 6951:24, 6960:18</p> <p>moments ^[3] - 6901:7, 6919:6, 6930:24</p> <p>Monday ^[1] - 6920:13</p> <p>Monet ^[1] - 6793:5</p> <p>money ^[10] - 6788:21, 6841:11, 6849:20, 6880:15, 6915:6, 6915:9, 6915:13, 6915:17, 6939:7, 6939:22</p> <p>monopolist ^[6] - 6824:25, 6825:6, 6825:10, 6825:19, 6825:20, 6963:10</p> <p>monopoly ^[4] - 6832:25, 6833:2, 6833:4, 6934:22</p> <p>Montana ^[1] - 6933:14</p> <p>months ^[1] - 6936:13</p> <p>Moore ^[1] - 6893:20</p> <p>MOORE ^[1] - 6773:11</p> <p>morgan ^[1] - 6796:8</p> <p>Morgan ^[4] - 6795:1, 6889:7, 6901:11, 6903:24</p> <p>morning ^[23] - 6774:7, 6774:9, 6774:12, 6774:18, 6774:21, 6774:22, 6774:25, 6775:2, 6775:4, 6775:6, 6775:8, 6775:11, 6775:13, 6775:16, 6775:18, 6775:19, 6778:11, 6866:20, 6871:2, 6871:14, 6879:25, 6894:22, 6931:25</p> <p>most ^[17] - 6825:15, 6830:14, 6833:12, 6836:5, 6849:13, 6874:14, 6888:17, 6891:23, 6893:11, 6933:9, 6938:4, 6939:14, 6952:5, 6959:14, 6962:9</p> <p>motion ^[1] - 6820:20</p> <p>motivated ^[1] - 6819:19</p> <p>move ^[9] - 6781:11, 6799:14, 6809:6, 6869:7, 6872:7, 6878:7, 6917:19, 6945:20, 6946:2</p> <p>moved ^[3] - 6799:12, 6809:14, 6945:20</p> <p>moving ^[10] - 6788:16, 6788:22, 6791:25, 6792:18, 6797:23, 6798:9, 6802:11, 6802:12, 6809:18, 6856:9</p>	<p>multiple ^[1] - 6932:9</p> <p>multiply ^[1] - 6827:14</p> <p>Music ^[1] - 6858:4</p> <p>must ^[15] - 6846:18, 6869:6, 6869:9, 6869:16, 6878:17, 6894:9, 6899:17, 6900:2, 6913:12, 6913:13, 6940:24, 6941:4, 6942:2, 6945:1, 6953:9</p>	<p>6805:16, 6805:19, 6805:24, 6806:4, 6806:8, 6807:9, 6807:24, 6808:16, 6808:18, 6820:2, 6862:24, 6863:12, 6877:23, 6878:20, 6878:22, 6878:23, 6879:13, 6879:15, 6881:1, 6881:3, 6882:1, 6902:19, 6902:22, 6905:8, 6950:16, 6951:1, 6951:2, 6955:4, 6957:6, 6963:9</p> <p>network-effect ^[2] - 6902:19, 6902:22</p> <p>networks ^[38] - 6778:20, 6780:12, 6781:6, 6782:2, 6787:15, 6787:17, 6788:12, 6788:24, 6789:6, 6790:24, 6795:17, 6796:6, 6806:1, 6806:12, 6806:14, 6807:16, 6811:2, 6811:25, 6816:15, 6816:16, 6824:15, 6824:20, 6832:2, 6834:24, 6835:13, 6838:4, 6863:8, 6863:9, 6867:19, 6902:17, 6917:12, 6918:13, 6923:17, 6923:20, 6924:3, 6935:18, 6950:24, 6960:1</p> <p>neutral ^[1] - 6858:19</p> <p>never ^[15] - 6810:3, 6830:5, 6867:10, 6871:3, 6872:19, 6874:23, 6878:14, 6881:20, 6889:9, 6890:5, 6903:2, 6903:12, 6908:3, 6920:7</p> <p>NEW ^[1] - 6772:1</p> <p>New ^[16] - 6772:23, 6773:12, 6773:16, 6830:16, 6830:20, 6831:15, 6832:1, 6832:7, 6904:19, 6912:16, 6928:23, 6928:24, 6928:25, 6965:15</p> <p>new ^[15] - 6791:7, 6791:25, 6792:9, 6793:25, 6794:2, 6809:14, 6810:3, 6812:14, 6821:13, 6841:3, 6871:3, 6874:1, 6885:4, 6899:16, 6942:12</p> <p>Newark ^[3] - 6846:8, 6846:9, 6848:6</p> <p>news ^[1] - 6866:20</p> <p>newspaper ^[3] - 6803:21, 6803:23, 6807:25</p> <p>newspapers ^[1] - 6816:9</p> <p>newsstand ^[1] - 6927:19</p> <p>next ^[24] - 6780:20, 6782:17, 6787:1, 6804:20, 6806:15, 6806:16, 6812:22, 6819:24, 6829:20, 6840:24, 6851:15, 6853:10, 6855:12, 6864:12, 6895:14, 6901:13, 6920:4, 6920:5, 6921:24, 6922:20, 6942:24, 6957:18, 6961:7</p> <p>NGG)(RER ^[2] - 6772:8, 6772:15</p> <p>niche ^[5] - 6889:16, 6889:17, 6901:19, 6905:3, 6927:7</p> <p>NICHOLAS ^[3] - 6772:20, 6774:2, 6823:2</p> <p>nickel ^[1] - 6883:24</p> <p>night ^[1] - 6909:20</p> <p>nine ^[2] - 6906:5, 6940:25</p> <p>nine-point-some ^[1] - 6940:25</p> <p>nineteen ^[1] - 6958:3</p> <p>nobody ^[4] - 6791:15, 6811:5, 6924:12, 6957:12</p> <p>nobody's ^[1] - 6959:20</p> <p>non ^[1] - 6926:19</p> <p>non-T&E ^[1] - 6926:19</p> <p>noncharge ^[1] - 6914:24</p>
N		
<p>N.Y ^[1] - 6772:9</p> <p>name ^[4] - 6866:21, 6939:12, 6956:22, 6961:11</p> <p>namely ^[3] - 6872:16, 6874:15, 6880:12</p> <p>narrow ^[2] - 6800:17, 6960:10</p> <p>narrower ^[2] - 6828:3, 6963:7</p> <p>National ^[2] - 6858:24, 6899:6</p> <p>natural ^[2] - 6883:2, 6883:4</p> <p>naturally ^[2] - 6797:24, 6857:6</p> <p>nature ^[1] - 6866:25</p> <p>naught ^[1] - 6902:6</p> <p>NDP ^[1] - 6896:10</p> <p>NDP's ^[3] - 6907:18, 6908:1, 6908:7</p> <p>NDPs ^[12] - 6796:11, 6869:13, 6870:19, 6870:23, 6872:10, 6885:9, 6886:4, 6887:4, 6887:5, 6894:16, 6947:5, 6954:4</p> <p>near ^[3] - 6890:1, 6904:22, 6942:18</p> <p>necessarily ^[2] - 6817:11, 6836:25</p> <p>necessary ^[4] - 6781:20, 6790:11, 6862:7, 6871:15</p> <p>necessity ^[1] - 6940:22</p> <p>need ^[34] - 6776:20, 6781:21, 6789:17, 6789:18, 6790:22, 6792:15, 6792:21, 6796:24, 6799:14, 6802:1, 6810:23, 6810:24, 6811:5, 6819:7, 6822:18, 6826:14, 6827:12, 6835:18, 6856:6, 6856:11, 6859:10, 6862:8, 6862:9, 6876:23, 6878:5, 6891:12, 6900:18, 6901:2, 6926:9, 6936:22, 6963:24, 6966:10</p> <p>needed ^[1] - 6778:18</p> <p>needs ^[1] - 6861:24</p> <p>negated ^[1] - 6842:1</p> <p>negative ^[3] - 6837:21, 6906:23, 6906:24</p> <p>negligible ^[2] - 6839:16, 6839:17</p> <p>negotiate ^[3] - 6781:25, 6921:22, 6942:10</p> <p>negotiated ^[7] - 6846:5, 6847:19, 6847:21, 6848:20, 6849:16, 6849:17, 6849:23</p> <p>negotiating ^[1] - 6922:3</p> <p>negotiation ^[1] - 6852:21</p> <p>negotiations ^[5] - 6922:11, 6923:4, 6923:6, 6923:12, 6936:8</p> <p>net ^[12] - 6802:2, 6814:18, 6817:1, 6817:2, 6817:3, 6817:5, 6841:1, 6844:4, 6852:17, 6919:20, 6936:16</p> <p>network ^[40] - 6785:13, 6786:8, 6786:15, 6788:18, 6789:15, 6791:3, 6793:6, 6795:16, 6805:1, 6805:12,</p>		

noncompliance ^[1] - 6785:11 nondiscrimination ^[3] - 6868:1, 6869:24, 6907:9 none ^[5] - 6801:10, 6827:3, 6827:5, 6902:8, 6939:1 nonprofit ^[1] - 6890:7 nonrevolvers ^[1] - 6914:19 nonrevolving ^[2] - 6914:4, 6914:12 nontrivial ^[1] - 6790:17 normal ^[2] - 6780:13, 6811:17 normally ^[2] - 6780:14, 6811:17 not-for-profit ^[1] - 6818:7 note ^[6] - 6780:22, 6796:1, 6804:23, 6819:25, 6838:18, 6877:12 nothing ^[12] - 6779:10, 6779:15, 6817:14, 6881:15, 6881:16, 6897:7, 6897:15, 6913:15, 6916:12, 6917:4, 6944:14, 6965:21 nothing's ^[2] - 6942:2, 6942:4 notice ^[1] - 6806:5 noting ^[1] - 6825:11 notwithstanding ^[2] - 6846:15, 6940:4 number ^[11] - 6796:2, 6843:22, 6854:2, 6854:4, 6854:17, 6854:25, 6875:19, 6877:9, 6913:14, 6921:2, 6931:5 numbers ^[5] - 6829:8, 6842:20, 6926:13, 6932:9, 6936:15 nutshell ^[2] - 6802:6, 6802:7 NW ^[1] - 6773:3 NYU ^[1] - 6886:21	offers ^[5] - 6832:8, 6832:10, 6833:14, 6834:15, 6858:15 officer ^[1] - 6845:16 official ^[2] - 6793:19, 6847:9 Official ^[1] - 6793:21 officially ^[1] - 6865:6 offset ^[6] - 6803:9, 6807:17, 6811:17, 6812:17, 6812:21, 6815:16 offsets ^[1] - 6815:13 offsetting ^[3] - 6815:23, 6817:4, 6844:7 often ^[3] - 6830:11, 6832:20, 6899:21 often-repeated ^[1] - 6899:21 OHIO ^[1] - 6772:6 Ohio ^[1] - 6773:9 Oil ^[2] - 6793:11, 6793:12 old ^[2] - 6908:2, 6929:15 old-fashioned ^[1] - 6929:15 once ^[5] - 6825:4, 6869:2, 6926:14, 6926:15, 6947:20 one ^[167] - 6777:12, 6780:6, 6781:4, 6782:9, 6782:12, 6782:21, 6784:14, 6791:9, 6792:3, 6801:22, 6801:25, 6802:16, 6803:9, 6803:15, 6803:24, 6805:10, 6805:14, 6806:14, 6806:25, 6807:16, 6808:23, 6810:15, 6814:11, 6815:7, 6815:9, 6820:11, 6827:10, 6828:9, 6830:4, 6830:13, 6830:19, 6832:24, 6832:25, 6835:1, 6835:20, 6836:21, 6838:25, 6841:17, 6841:18, 6841:19, 6844:25, 6845:14, 6847:4, 6847:9, 6848:7, 6850:9, 6850:10, 6850:23, 6851:6, 6852:23, 6853:7, 6853:11, 6853:24, 6855:2, 6856:5, 6856:24, 6857:24, 6860:18, 6865:4, 6865:5, 6865:11, 6865:13, 6866:19, 6869:20, 6870:11, 6871:9, 6871:16, 6871:19, 6871:20, 6873:4, 6873:15, 6875:20, 6875:23, 6876:20, 6877:6, 6878:22, 6879:2, 6879:9, 6879:10, 6879:20, 6879:21, 6880:9, 6881:18, 6882:4, 6882:8, 6882:10, 6885:11, 6886:3, 6886:25, 6888:6, 6888:14, 6888:22, 6889:13, 6889:22, 6891:19, 6891:21, 6891:24, 6891:25, 6893:19, 6897:10, 6897:11, 6897:25, 6898:5, 6899:5, 6899:8, 6899:13, 6902:21, 6909:13, 6909:14, 6912:7, 6912:8, 6912:18, 6913:5, 6913:6, 6913:12, 6913:13, 6913:16, 6913:23, 6913:24, 6914:24, 6915:3, 6916:22, 6917:12, 6917:14, 6919:20, 6919:22, 6920:1, 6921:5, 6921:15, 6924:1, 6924:18, 6924:23, 6929:4, 6930:6, 6930:11, 6931:1, 6933:8, 6935:11, 6936:11, 6937:2, 6940:12, 6940:18, 6944:6, 6948:5, 6948:16, 6948:21, 6948:25, 6951:16, 6951:17, 6954:20, 6959:19, 6960:8, 6960:10, 6961:7, 6961:13, 6962:4, 6962:5, 6964:19, 6964:23, 6965:8, 6965:25, 6966:15 one's ^[2] - 6804:18	one-fifth ^[1] - 6889:22 one-sided ^[1] - 6885:11 one-third ^[2] - 6891:24, 6891:25 ones ^[1] - 6812:7 online ^[1] - 6791:4 oooooooOooooooo ^[1] - 6967:7 open ^[4] - 6774:1, 6823:1, 6865:2, 6949:14 opening ^[4] - 6820:21, 6868:22, 6894:17, 6940:19 openings ^[1] - 6777:11 operandi ^[1] - 6954:13 operating ^[2] - 6782:21, 6845:15 operation ^[2] - 6790:15, 6927:5 operations ^[1] - 6835:6 opinion ^[13] - 6825:5, 6869:17, 6872:2, 6875:23, 6876:19, 6876:25, 6877:1, 6912:19, 6950:8, 6953:20, 6953:21, 6962:12, 6966:7 opportunity ^[9] - 6778:17, 6779:20, 6791:18, 6811:15, 6819:10, 6863:3, 6908:20, 6946:3, 6946:4 opposed ^[5] - 6814:3, 6822:7, 6831:17, 6870:21, 6881:7 opposing ^[1] - 6882:2 opposite ^[4] - 6852:12, 6902:14, 6932:11, 6937:1 Optima ^[1] - 6798:7 option ^[2] - 6793:7, 6843:1 options ^[1] - 6785:22 oral ^[2] - 6774:5, 6775:20 orange ^[1] - 6853:19 oranges ^[2] - 6850:12, 6850:20 order ^[16] - 6819:2, 6828:15, 6848:14, 6848:24, 6856:6, 6856:11, 6896:5, 6907:9, 6913:14, 6914:9, 6914:17, 6923:6, 6937:3, 6944:3, 6958:11, 6960:16 ordinary ^[2] - 6804:18, 6804:21 originally ^[2] - 6779:11, 6874:7 Orsini ^[1] - 6775:3 ORSINI ^[2] - 6773:13, 6775:2 otherwise ^[3] - 6777:25, 6789:23, 6918:17 ought ^[8] - 6810:19, 6811:18, 6826:8, 6836:15, 6836:18, 6838:11, 6839:10, 6952:20 outcome ^[5] - 6789:18, 6789:19, 6810:23, 6811:3, 6871:9 output ^[4] - 6800:12, 6877:18, 6877:20, 6877:23 outweigh ^[1] - 6812:3 overall ^[7] - 6788:5, 6788:8, 6817:6, 6839:20, 6841:19, 6877:18, 6916:7 overcome ^[1] - 6932:22 overlapping ^[3] - 6796:6, 6893:25, 6915:19 overstated ^[1] - 6959:7 overtake ^[1] - 6956:11 overwhelming ^[1] - 6953:18 own ^[20] - 6809:22, 6829:22, 6836:23,
O		
oath ^[3] - 6867:5, 6883:23, 6937:7 objective ^[2] - 6834:6, 6954:16 obscure ^[2] - 6824:4, 6965:3 observation ^[1] - 6906:7 observe ^[2] - 6941:11, 6961:24 observed ^[4] - 6917:19, 6953:3, 6953:4, 6962:2 observer ^[1] - 6875:11 obstruct ^[1] - 6783:18 obtain ^[1] - 6787:24 obviate ^[2] - 6876:23, 6900:17 obvious ^[2] - 6830:14, 6913:6 obviously ^[6] - 6783:8, 6865:25, 6873:11, 6873:18, 6912:24, 6934:23 occurred ^[2] - 6865:2, 6949:14 October ^[1] - 6772:17 OF ^[9] - 6772:1, 6772:3, 6772:4, 6772:4, 6772:5, 6772:5, 6772:6, 6772:6, 6772:7 offending ^[2] - 6857:2, 6857:14 offer ^[14] - 6780:18, 6785:22, 6813:24, 6814:22, 6819:11, 6861:9, 6861:23, 6886:25, 6950:14, 6958:11, 6958:25, 6959:1, 6959:3, 6959:16 offered ^[6] - 6786:8, 6812:15, 6812:20, 6825:5, 6834:14, 6953:12 offering ^[4] - 6788:17, 6814:12, 6898:17, 6898:18		

6843:12, 6846:8, 6846:17, 6848:8, 6848:14, 6857:10, 6861:25, 6881:20, 6885:12, 6888:22, 6890:17, 6907:9, 6923:22, 6937:23, 6941:13, 6946:2 owned [5] - 6793:6, 6890:8, 6893:24, 6932:3, 6932:7	6824:23, 6946:4, 6952:18, 6964:18 Pause [1] - 6898:24 pause [4] - 6877:6, 6877:17, 6914:6, 6917:13 pay [33] - 6782:19, 6782:24, 6803:3, 6812:7, 6812:8, 6812:9, 6825:21, 6826:1, 6826:16, 6827:12, 6828:13, 6837:7, 6837:15, 6839:10, 6843:10, 6845:19, 6849:19, 6849:20, 6863:16, 6894:16, 6894:18, 6914:15, 6914:16, 6914:17, 6915:13, 6917:22, 6936:5, 6936:10, 6937:25, 6938:1, 6939:8, 6950:4 paying [13] - 6828:12, 6836:15, 6841:9, 6843:20, 6843:23, 6852:10, 6852:13, 6853:5, 6853:6, 6853:7, 6863:17, 6881:7, 6885:14 payment [7] - 6790:23, 6791:7, 6792:4, 6852:18, 6858:4, 6918:25, 6924:2 Payments [2] - 6793:19, 6793:21 payments [3] - 6852:16, 6853:1, 6960:4 PayPal [6] - 6790:3, 6791:1, 6791:5, 6791:13, 6866:20, 6866:23 pays [2] - 6826:2, 6881:6 pen [2] - 6913:15, 6913:16 penalties [2] - 6845:20, 6849:21 people [28] - 6788:22, 6792:16, 6808:12, 6827:12, 6831:25, 6832:13, 6842:21, 6842:25, 6845:9, 6852:5, 6898:17, 6902:10, 6909:12, 6914:14, 6917:5, 6917:20, 6920:12, 6935:21, 6937:5, 6937:10, 6939:18, 6939:25, 6944:15, 6963:4, 6963:21, 6964:3, 6964:4 per [3] - 6874:4, 6874:7, 6875:15 perceived [1] - 6958:10 percent [65] - 6794:25, 6799:20, 6799:25, 6800:19, 6835:5, 6839:15, 6850:15, 6852:10, 6854:3, 6854:5, 6854:6, 6854:16, 6884:13, 6884:17, 6884:18, 6884:19, 6892:19, 6893:1, 6893:7, 6893:16, 6898:3, 6905:12, 6906:2, 6908:4, 6909:1, 6910:5, 6910:8, 6910:21, 6910:22, 6910:23, 6911:3, 6913:1, 6920:22, 6920:23, 6922:8, 6922:10, 6924:20, 6924:21, 6925:10, 6926:6, 6926:19, 6928:4, 6931:3, 6931:4, 6931:6, 6931:12, 6931:13, 6931:15, 6932:17, 6942:3, 6942:4, 6942:5, 6942:7, 6942:14, 6943:4, 6955:2, 6955:12, 6956:20, 6957:6, 6958:3 percentage [5] - 6800:17, 6891:24, 6923:13, 6931:13, 6931:22 perceptions [3] - 6906:1, 6907:2, 6907:3 perfect [12] - 6789:10, 6790:18, 6913:13, 6913:19, 6913:25, 6914:7, 6914:8, 6914:20, 6915:18, 6915:23, 6916:10 perfectly [3] - 6782:16, 6858:18,	6959:21 perhaps [8] - 6798:5, 6798:25, 6865:13, 6873:21, 6879:24, 6902:18, 6908:14, 6955:12 period [9] - 6777:12, 6787:4, 6787:5, 6789:12, 6798:17, 6842:15, 6851:6, 6853:21, 6895:6 permit [2] - 6796:14, 6802:14 permits [1] - 6814:4 perpetrated [1] - 6868:4 perpetuated [1] - 6903:6 person [3] - 6826:2, 6832:6, 6885:17 person's [1] - 6875:24 personally [2] - 6937:10, 6938:5 perspective [6] - 6830:24, 6835:17, 6837:2, 6916:3, 6916:6, 6959:12 persuaded [1] - 6936:14 pesky [1] - 6889:15 PETER [2] - 6773:14, 6773:20 Peter [1] - 6775:14 phase [1] - 6966:3 Philadelphia [1] - 6899:6 PHILIP [1] - 6773:18 Philip [1] - 6775:9 phone [1] - 6792:7 phones [1] - 6792:4 phrase [6] - 6837:20, 6849:20, 6877:24, 6879:25, 6910:15, 6931:24 physician [1] - 6900:14 physicians' [1] - 6900:13 Picayune [2] - 6803:20, 6808:22 picture [3] - 6797:5, 6802:17, 6951:24 piece [2] - 6876:20, 6927:6 pieces [5] - 6835:25, 6836:2, 6876:20, 6879:15, 6923:12 pile [1] - 6927:8 place [10] - 6828:17, 6832:4, 6856:18, 6902:1, 6905:11, 6933:19, 6945:13, 6950:16, 6959:18, 6961:12 places [5] - 6797:3, 6848:1, 6848:12, 6874:10, 6917:9 Plaintiff [2] - 6773:2, 6774:23 plaintiff [12] - 6811:14, 6815:24, 6862:19, 6864:4, 6870:6, 6876:6, 6876:12, 6876:14, 6882:19, 6896:5, 6900:14, 6928:16 plaintiffs [2] - 6900:5, 6900:8 plaintiffs [8] - 6775:23, 6808:5, 6815:20, 6816:11, 6816:12, 6817:2, 6817:8, 6896:9 Plaintiffs [1] - 6772:8 plaintiffs' [1] - 6804:8 Plaintiffs' [1] - 6865:10 plan [1] - 6821:3 planning [3] - 6838:18, 6888:23, 6901:12 plastic [5] - 6880:13, 6940:23, 6941:8, 6941:9, 6954:7 platform [6] - 6803:9, 6807:24, 6816:9, 6817:6, 6951:1, 6951:2 platitudes [1] - 6945:8
P		
p.m [1] - 6864:9 package [3] - 6849:3, 6861:23, 6958:8 page [13] - 6802:10, 6802:24, 6812:22, 6826:20, 6853:10, 6855:12, 6864:12, 6895:14, 6905:24, 6922:20, 6943:6, 6950:9, 6957:18 PAGE [1] - 6968:3 pages [2] - 6802:13, 6937:15 pain [1] - 6937:8 pair [4] - 6831:2, 6831:8, 6928:20, 6928:23 pairs [3] - 6830:16, 6879:8, 6965:9 pants [2] - 6879:8, 6879:16 paper [2] - 6865:22, 6866:1 papers [12] - 6801:24, 6827:25, 6845:25, 6866:15, 6867:14, 6871:13, 6871:14, 6912:11, 6932:14, 6944:2, 6949:21, 6966:11 parade [3] - 6946:24, 6947:4, 6947:15 paradigm [1] - 6903:19 parallel [1] - 6950:8 parameters [1] - 6919:11 Parish [1] - 6876:3 part [34] - 6781:14, 6784:12, 6784:16, 6788:16, 6789:14, 6796:2, 6799:10, 6804:8, 6805:3, 6827:9, 6831:9, 6836:6, 6836:7, 6836:8, 6836:9, 6845:7, 6845:8, 6848:9, 6848:25, 6850:23, 6851:6, 6854:6, 6866:23, 6878:10, 6879:2, 6887:16, 6918:9, 6921:6, 6942:25, 6954:20, 6956:1, 6956:5, 6959:9 participant [1] - 6820:9 participants [1] - 6811:1 participation [1] - 6849:15 particular [17] - 6789:17, 6803:14, 6810:23, 6810:24, 6819:11, 6832:21, 6836:4, 6836:5, 6836:13, 6836:20, 6837:7, 6849:11, 6850:4, 6853:18, 6897:1, 6915:6, 6954:23 particularized [1] - 6831:14 particularly [1] - 6832:13 parties [8] - 6775:20, 6790:13, 6790:14, 6849:23, 6866:11, 6869:18, 6872:3, 6966:5 partner [2] - 6852:22, 6942:23 parts [5] - 6777:24, 6784:11, 6785:21, 6954:18, 6959:6 party [2] - 6805:20, 6819:14 pass [3] - 6816:17, 6819:21, 6883:25 passed [3] - 6816:20, 6863:14, 6883:24 passing [1] - 6818:7 past [7] - 6787:22, 6788:11, 6792:23,		

<p>plausible [1] - 6893:11</p> <p>play [1] - 6885:10</p> <p>playbook [3] - 6889:13, 6898:13, 6903:17</p> <p>player [1] - 6854:4</p> <p>players [1] - 6918:20</p> <p>plays [2] - 6838:4, 6867:8</p> <p>Plaza [2] - 6772:23, 6773:11</p> <p>plenty [2] - 6801:20, 6829:18</p> <p>plus [10] - 6872:20, 6872:23, 6881:14, 6883:5, 6884:22, 6885:13, 6891:2, 6892:10, 6908:12, 6941:2</p> <p>pocket [1] - 6929:3</p> <p>pockets [1] - 6880:14</p> <p>point [57] - 6777:23, 6784:10, 6785:10, 6786:10, 6792:5, 6794:11, 6795:18, 6797:7, 6800:5, 6807:5, 6816:6, 6818:10, 6819:24, 6820:11, 6825:13, 6829:19, 6841:2, 6850:6, 6850:9, 6850:10, 6858:16, 6858:17, 6879:25, 6886:9, 6887:1, 6888:7, 6889:14, 6890:13, 6890:15, 6890:20, 6904:1, 6904:25, 6906:23, 6906:25, 6910:8, 6911:13, 6914:22, 6915:8, 6915:16, 6919:2, 6919:15, 6919:17, 6927:9, 6928:24, 6929:24, 6934:18, 6940:25, 6942:15, 6947:19, 6956:9, 6960:10, 6961:4, 6962:16, 6966:11</p> <p>pointed [5] - 6876:6, 6878:22, 6887:11, 6912:2, 6918:24</p> <p>pointing [3] - 6866:14, 6890:7, 6896:25</p> <p>points [13] - 6783:6, 6788:11, 6839:24, 6840:1, 6844:25, 6897:2, 6899:2, 6916:18, 6918:2, 6925:5, 6931:22, 6937:25</p> <p>Pojero [2] - 6933:7, 6936:3</p> <p>politically [1] - 6910:14</p> <p>poor [1] - 6863:16</p> <p>portion [3] - 6876:25, 6877:1, 6950:7</p> <p>portions [1] - 6866:13</p> <p>posed [2] - 6923:24, 6947:13</p> <p>posited [1] - 6809:2</p> <p>position [16] - 6778:25, 6817:15, 6835:4, 6843:8, 6843:17, 6843:24, 6868:16, 6891:15, 6892:4, 6902:2, 6918:6, 6947:18, 6955:13, 6957:16, 6958:12, 6958:17</p> <p>possibilities [2] - 6792:3, 6807:21</p> <p>possibility [4] - 6779:24, 6794:9, 6826:12, 6877:22</p> <p>possible [10] - 6779:5, 6790:1, 6801:13, 6815:18, 6828:10, 6829:7, 6953:7, 6953:8, 6953:9, 6953:13</p> <p>possibly [1] - 6953:17</p> <p>post [7] - 6779:3, 6781:10, 6801:24, 6869:7, 6872:7, 6878:8, 6945:21</p> <p>post-trial [3] - 6779:3, 6781:10, 6801:24</p> <p>posted [1] - 6947:3</p> <p>poster [1] - 6931:23</p> <p>posture [1] - 6954:9</p> <p>potential [2] - 6831:10, 6849:10</p>	<p>power [56] - 6838:14, 6838:20, 6839:1, 6839:6, 6844:18, 6854:2, 6854:6, 6854:10, 6854:13, 6855:10, 6855:11, 6871:17, 6876:24, 6898:2, 6906:8, 6910:1, 6910:2, 6913:4, 6913:8, 6916:18, 6925:2, 6928:3, 6928:5, 6928:7, 6929:8, 6929:11, 6929:13, 6929:14, 6929:25, 6930:7, 6930:9, 6930:13, 6930:14, 6931:19, 6931:21, 6932:18, 6933:1, 6933:2, 6934:4, 6934:16, 6934:21, 6934:22, 6936:6, 6936:23, 6936:25, 6937:4, 6940:8, 6940:10, 6940:13, 6940:18, 6941:10, 6941:18, 6941:19, 6944:3</p> <p>powerless [1] - 6945:4</p> <p>powers [1] - 6854:14</p> <p>practical [2] - 6955:16, 6964:7</p> <p>practice [2] - 6820:20, 6966:9</p> <p>pre [1] - 6852:18</p> <p>Pre [3] - 6820:21, 6840:17, 6850:11</p> <p>pre-payment [1] - 6852:18</p> <p>Pre-Tax [2] - 6840:17, 6850:11</p> <p>Pre-Trial [1] - 6820:21</p> <p>precedent [2] - 6944:25, 6945:1</p> <p>precisely [3] - 6829:18, 6868:1, 6945:18</p> <p>predict [1] - 6884:24</p> <p>predicted [1] - 6887:21</p> <p>preempt [1] - 6889:2</p> <p>prefer [5] - 6778:1, 6795:4, 6799:23, 6814:16, 6859:18</p> <p>Prefer [12] - 6868:3, 6894:11, 6901:8, 6904:2, 6904:3, 6904:8, 6904:11, 6905:10, 6905:22, 6905:23, 6906:4, 6945:18</p> <p>preference [13] - 6777:13, 6794:22, 6795:13, 6795:15, 6795:16, 6795:20, 6798:18, 6800:10, 6836:23, 6836:24, 6857:20, 6875:24, 6901:19</p> <p>preferred [4] - 6836:13, 6836:14, 6836:15, 6836:18</p> <p>prefers [1] - 6837:1</p> <p>premise [1] - 6959:7</p> <p>premised [1] - 6868:23</p> <p>premium [7] - 6788:6, 6868:6, 6896:25, 6897:21, 6901:18, 6934:11, 6953:15</p> <p>prepared [1] - 6914:16</p> <p>prepurchase [2] - 6852:21, 6853:2</p> <p>prescriptions [1] - 6911:8</p> <p>present [2] - 6788:4, 6884:23</p> <p>presentation [16] - 6777:18, 6777:19, 6777:24, 6804:21, 6805:14, 6806:19, 6823:17, 6828:19, 6864:10, 6865:10, 6865:23, 6876:7, 6876:15, 6917:16, 6917:17, 6917:25</p> <p>presentations [1] - 6889:10</p> <p>presenting [1] - 6821:11</p> <p>preserved [1] - 6903:6</p> <p>president [2] - 6845:15, 6918:16</p> <p>press [2] - 6883:11, 6883:15</p> <p>pressure [2] - 6798:14, 6901:14</p> <p>pressures [1] - 6818:3</p>	<p>presumably [2] - 6848:21, 6848:25</p> <p>presume [1] - 6910:24</p> <p>presumption [3] - 6932:18, 6932:19, 6932:23</p> <p>pretext [1] - 6902:13</p> <p>pretty [6] - 6780:9, 6851:23, 6876:21, 6912:21, 6927:6, 6946:7</p> <p>prevail [2] - 6816:11, 6817:8</p> <p>prevailed [1] - 6882:13</p> <p>prevent [4] - 6856:11, 6863:1, 6911:15, 6944:23</p> <p>previous [1] - 6829:21</p> <p>price [181] - 6780:11, 6780:14, 6781:5, 6781:14, 6781:25, 6782:1, 6783:18, 6784:2, 6784:5, 6784:7, 6785:23, 6786:1, 6786:11, 6786:12, 6786:14, 6786:15, 6786:16, 6786:18, 6786:24, 6787:3, 6787:5, 6787:12, 6787:14, 6787:16, 6787:20, 6787:21, 6787:22, 6789:1, 6789:17, 6792:23, 6793:13, 6793:14, 6793:15, 6794:2, 6794:20, 6795:2, 6795:5, 6795:7, 6795:21, 6795:22, 6795:24, 6795:25, 6799:25, 6800:6, 6800:9, 6801:16, 6806:7, 6807:15, 6808:9, 6808:10, 6810:9, 6810:24, 6814:2, 6814:3, 6820:8, 6824:18, 6824:20, 6825:20, 6825:21, 6825:22, 6826:1, 6827:20, 6828:2, 6828:10, 6828:15, 6829:4, 6829:6, 6835:23, 6838:7, 6839:13, 6840:15, 6840:17, 6840:18, 6840:20, 6840:21, 6840:23, 6841:3, 6841:5, 6841:8, 6841:10, 6842:1, 6843:18, 6844:17, 6844:22, 6845:3, 6845:4, 6845:13, 6846:3, 6847:11, 6850:4, 6850:13, 6851:10, 6851:20, 6851:22, 6851:23, 6851:24, 6853:5, 6854:23, 6855:1, 6855:3, 6860:1, 6860:2, 6860:5, 6860:7, 6861:21, 6862:23, 6870:6, 6870:18, 6872:10, 6872:13, 6872:14, 6873:7, 6873:9, 6873:12, 6874:8, 6874:9, 6876:2, 6876:11, 6876:12, 6876:13, 6877:10, 6877:24, 6878:6, 6882:12, 6882:14, 6882:19, 6882:21, 6882:24, 6883:1, 6885:22, 6894:22, 6895:9, 6895:10, 6895:11, 6896:5, 6896:7, 6896:14, 6896:20, 6896:24, 6897:4, 6897:5, 6899:24, 6900:5, 6901:18, 6916:17, 6917:1, 6924:12, 6924:13, 6925:13, 6925:15, 6925:16, 6925:17, 6925:19, 6926:10, 6934:6, 6934:7, 6937:4, 6938:11, 6939:23, 6940:11, 6951:7, 6951:19, 6951:21, 6952:2, 6952:5, 6952:8, 6952:12, 6952:13, 6952:17, 6952:23, 6953:8, 6958:10, 6961:3, 6962:13, 6963:10, 6963:11</p> <p>price-related [2] - 6924:12, 6924:13</p> <p>priced [6] - 6786:8, 6788:19, 6791:23, 6793:7, 6814:11, 6960:10</p> <p>prices [92] - 6780:18, 6781:2, 6781:13, 6784:7, 6785:9, 6785:13, 6785:14,</p>
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<p>6785:17, 6786:9, 6787:9, 6787:10, 6787:12, 6787:25, 6789:3, 6789:4, 6789:22, 6793:16, 6795:11, 6800:7, 6800:8, 6800:9, 6801:9, 6803:3, 6807:2, 6812:1, 6812:8, 6812:17, 6812:19, 6816:16, 6816:17, 6816:24, 6817:3, 6817:19, 6817:20, 6820:5, 6824:16, 6828:5, 6828:12, 6828:13, 6828:14, 6829:14, 6835:12, 6839:11, 6839:15, 6841:19, 6842:5, 6844:6, 6850:25, 6851:5, 6851:10, 6851:18, 6853:14, 6853:20, 6854:24, 6859:23, 6860:25, 6863:15, 6876:16, 6884:22, 6894:20, 6894:24, 6895:9, 6896:2, 6896:4, 6896:19, 6896:22, 6896:23, 6897:8, 6897:20, 6897:24, 6900:20, 6925:19, 6926:22, 6951:9, 6951:20, 6952:14, 6952:15, 6952:17, 6953:11, 6953:15, 6953:22, 6954:1, 6958:11, 6958:16, 6959:3, 6959:16, 6959:18, 6959:19, 6962:7</p> <p>pricing [12] - 6780:13, 6781:22, 6788:4, 6788:5, 6858:17, 6862:9, 6873:11, 6873:18, 6877:3, 6900:18, 6934:4, 6934:25</p> <p>Priebe [3] - 6780:8, 6781:23, 6792:10</p> <p>primarily [2] - 6783:16, 6854:19</p> <p>primary [1] - 6846:11</p> <p>principal [3] - 6867:4, 6867:13, 6869:3</p> <p>principle [16] - 6779:13, 6783:25, 6785:19, 6794:6, 6810:22, 6810:24, 6882:21, 6899:16, 6899:17, 6926:6, 6926:7, 6950:18, 6953:10, 6953:12, 6965:20</p> <p>principles [3] - 6783:14, 6824:10, 6951:11</p> <p>prisoners [2] - 6880:18, 6938:8</p> <p>private [1] - 6896:8</p> <p>privilege [2] - 6852:10, 6852:13</p> <p>pro [10] - 6795:10, 6798:10, 6811:11, 6811:16, 6811:18, 6815:2, 6859:4, 6860:4, 6868:18, 6883:13</p> <p>pro-competitive [10] - 6795:10, 6798:10, 6811:11, 6811:16, 6811:18, 6815:2, 6859:4, 6860:4, 6868:18, 6883:13</p> <p>probable [2] - 6953:20, 6953:22</p> <p>problem [9] - 6790:19, 6845:11, 6878:10, 6878:11, 6900:23, 6913:8, 6928:2, 6929:10, 6933:12</p> <p>problems [3] - 6798:16, 6827:7, 6933:16</p> <p>procedural [1] - 6948:23</p> <p>procedurally [2] - 6948:5, 6948:22</p> <p>proceed [4] - 6778:7, 6823:7, 6865:16, 6898:25</p> <p>proceeding [4] - 6920:7, 6948:1, 6966:5, 6966:11</p> <p>proceedings [3] - 6888:7, 6948:7, 6948:12</p> <p>Proceedings [1] - 6772:24</p>	<p>process [21] - 6779:22, 6783:9, 6783:10, 6783:24, 6784:13, 6787:8, 6788:23, 6789:2, 6789:19, 6789:24, 6800:5, 6801:3, 6801:8, 6859:14, 6866:1, 6886:12, 6907:15, 6945:12, 6951:8, 6951:17, 6952:10</p> <p>produced [2] - 6772:25, 6811:23</p> <p>produces [1] - 6852:8</p> <p>product [30] - 6806:20, 6819:11, 6819:15, 6824:18, 6867:8, 6870:1, 6873:10, 6873:19, 6873:21, 6873:22, 6875:24, 6880:8, 6880:11, 6880:21, 6897:5, 6897:12, 6898:17, 6901:19, 6907:3, 6916:22, 6921:9, 6935:14, 6935:17, 6944:7, 6944:8, 6944:11, 6945:1, 6945:2</p> <p>products [7] - 6863:15, 6863:18, 6881:8, 6923:23, 6939:14, 6953:11, 6962:15</p> <p>professional [2] - 6953:20, 6953:21</p> <p>Professional [1] - 6858:24</p> <p>Professor [49] - 6787:16, 6806:19, 6806:21, 6816:22, 6824:25, 6825:9, 6826:4, 6827:21, 6827:24, 6828:5, 6841:23, 6842:3, 6842:7, 6842:19, 6843:6, 6843:19, 6843:25, 6844:4, 6844:12, 6851:1, 6851:4, 6851:16, 6852:2, 6852:15, 6853:14, 6853:18, 6878:23, 6895:4, 6913:2, 6914:2, 6915:25, 6924:6, 6924:9, 6924:10, 6924:17, 6925:21, 6926:9, 6926:16, 6930:8, 6952:23, 6952:24, 6953:5, 6962:9, 6962:12, 6963:15, 6963:19, 6964:13, 6964:15, 6964:21</p> <p>professor [6] - 6803:13, 6806:24, 6825:4, 6844:8, 6853:13, 6853:15</p> <p>profile [1] - 6921:6</p> <p>profit [4] - 6795:4, 6818:7, 6819:19, 6881:10</p> <p>profitability [2] - 6821:6, 6822:3</p> <p>profitable [6] - 6842:6, 6844:17, 6844:20, 6881:11, 6934:22, 6965:17</p> <p>profits [11] - 6819:2, 6819:8, 6819:15, 6819:17, 6843:13, 6934:12, 6934:13, 6934:16, 6934:19, 6958:19</p> <p>program [22] - 6839:20, 6839:23, 6840:5, 6841:14, 6841:17, 6841:23, 6841:25, 6842:9, 6842:16, 6842:17, 6843:5, 6843:13, 6843:17, 6844:1, 6845:9, 6845:18, 6846:2, 6850:19, 6904:11, 6938:5</p> <p>programs [1] - 6950:15</p> <p>prohibited [1] - 6857:24</p> <p>prohibiting [1] - 6865:22</p> <p>Project [1] - 6793:5</p> <p>project [1] - 6886:8</p> <p>projections [1] - 6840:25</p> <p>prominent [1] - 6956:22</p> <p>promises [1] - 6848:25</p> <p>promising [1] - 6848:23</p> <p>promote [2] - 6954:16, 6954:17</p>	<p>promoting [1] - 6788:6</p> <p>promotion [1] - 6795:8</p> <p>promotions [1] - 6857:1</p> <p>prompting [2] - 6813:22, 6857:15</p> <p>proof [5] - 6801:18, 6838:18, 6854:7, 6897:15, 6951:20</p> <p>propensity [1] - 6905:14</p> <p>proper [6] - 6784:2, 6784:5, 6868:7, 6870:13, 6934:15, 6951:18</p> <p>property [1] - 6942:24</p> <p>proportion [1] - 6851:8</p> <p>proposal [1] - 6933:22</p> <p>proposals [1] - 6966:6</p> <p>propose [2] - 6938:18, 6966:12</p> <p>proposed [4] - 6831:11, 6872:12, 6926:12, 6944:23</p> <p>proposition [23] - 6801:11, 6802:4, 6803:6, 6803:7, 6816:7, 6819:3, 6827:25, 6829:21, 6830:8, 6830:10, 6896:3, 6899:7, 6899:10, 6926:21, 6926:24, 6927:11, 6932:21, 6945:1, 6951:16, 6959:11, 6963:6, 6964:11, 6965:7</p> <p>propositions [1] - 6782:6</p> <p>prosper [1] - 6902:16</p> <p>protect [16] - 6783:16, 6808:14, 6822:19, 6859:10, 6859:13, 6859:14, 6867:9, 6867:11, 6867:12, 6907:10, 6956:8, 6956:15, 6956:16, 6960:22</p> <p>protected [2] - 6783:19, 6819:7</p> <p>protecting [3] - 6843:12, 6946:9, 6946:10</p> <p>protection [2] - 6808:2, 6820:15</p> <p>protectionism [4] - 6811:7, 6859:11, 6907:24, 6907:25</p> <p>prove [47] - 6782:10, 6802:2, 6811:23, 6811:24, 6812:4, 6815:21, 6815:25, 6817:2, 6838:18, 6853:24, 6867:13, 6869:6, 6869:9, 6871:15, 6871:17, 6871:21, 6872:4, 6872:6, 6872:8, 6872:12, 6873:6, 6876:23, 6878:5, 6882:19, 6882:20, 6882:24, 6882:25, 6894:14, 6896:5, 6896:9, 6896:12, 6896:13, 6896:14, 6896:21, 6897:3, 6899:17, 6910:1, 6910:3, 6912:11, 6912:12, 6912:13, 6912:19, 6912:22, 6934:15, 6940:17</p> <p>proved [16] - 6800:4, 6800:13, 6801:16, 6812:2, 6838:23, 6853:23, 6871:16, 6871:17, 6872:13, 6872:14, 6881:15, 6900:25, 6913:17, 6934:7, 6951:7</p> <p>proven [5] - 6911:11, 6928:12, 6929:15, 6930:2, 6936:24</p> <p>proves [5] - 6811:14, 6870:24, 6897:4, 6897:6</p> <p>provide [6] - 6805:10, 6811:12, 6834:24, 6848:15, 6859:22, 6887:18</p> <p>provided [4] - 6779:5, 6858:17, 6865:7, 6881:18</p> <p>provides [1] - 6859:20</p> <p>providing [3] - 6939:13, 6939:22,</p>
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<p>6941:14 proving [1] - 6876:24 provision [3] - 6849:6, 6858:5, 6885:20 provisions [5] - 6868:1, 6869:24, 6869:25, 6907:9, 6919:9 provocative [1] - 6906:16 PTI [1] - 6840:17 public [8] - 6777:1, 6829:9, 6840:8, 6890:4, 6890:9, 6890:10, 6893:24, 6935:7 publication [1] - 6923:21 publicly [1] - 6909:21 publix [1] - 6936:8 Publix [1] - 6936:9 puffery [1] - 6839:7 pull [3] - 6792:6, 6845:6, 6845:8 pulled [2] - 6875:23, 6877:14 pulling [4] - 6792:8, 6845:23, 6846:1, 6846:2 pump [1] - 6793:13 punished [1] - 6846:1 purchase [5] - 6814:3, 6880:20, 6911:3, 6917:23, 6920:4 purchases [1] - 6919:25 pure [1] - 6915:11 purpose [4] - 6914:11, 6920:1, 6945:9, 6965:2 purposes [5] - 6896:6, 6896:7, 6896:23, 6921:21, 6923:22 pursue [2] - 6787:25, 6908:17 pursued [2] - 6779:21, 6908:16 pursuing [1] - 6908:6 push [1] - 6811:6 pushed [1] - 6937:23 pushes [1] - 6807:18 put [43] - 6775:21, 6783:23, 6791:13, 6793:1, 6798:14, 6804:1, 6804:4, 6815:24, 6821:20, 6822:18, 6838:16, 6852:6, 6858:1, 6861:6, 6865:6, 6869:13, 6875:22, 6877:10, 6883:9, 6889:11, 6890:3, 6890:15, 6893:7, 6894:22, 6907:21, 6909:14, 6912:25, 6913:20, 6914:4, 6914:18, 6919:4, 6919:7, 6921:25, 6923:18, 6924:14, 6925:9, 6931:16, 6940:16, 6946:5, 6958:17, 6959:13, 6961:10, 6963:10 puts [1] - 6915:21 putting [11] - 6799:22, 6804:6, 6804:10, 6804:12, 6808:22, 6871:11, 6896:25, 6905:2, 6907:23, 6937:20, 6959:13</p>	<p>quantitative [3] - 6924:12, 6924:13, 6924:22 quarter [1] - 6888:12 quarters [3] - 6893:6, 6910:18, 6920:17 questioning [1] - 6905:17 questions [6] - 6798:4, 6823:15, 6915:22, 6937:2, 6952:22, 6963:13 quick [15] - 6801:4, 6801:6, 6870:13, 6874:1, 6874:5, 6874:16, 6874:17, 6874:22, 6874:25, 6875:4, 6875:7, 6877:2, 6960:3, 6960:5 quick-look [2] - 6801:4, 6801:6 quicker [1] - 6916:6 quintessential [2] - 6875:3, 6875:4 quite [8] - 6780:19, 6807:22, 6867:1, 6920:10, 6923:14, 6934:13, 6934:14, 6936:25 quotation [1] - 6803:21 quote [9] - 6872:10, 6875:5, 6875:22, 6877:1, 6877:15, 6878:3, 6899:20, 6930:24 quoted [1] - 6816:22 quoting [2] - 6876:2, 6930:22</p>	<p>razor [2] - 6927:19, 6927:20 RE [1] - 6772:15 reach [4] - 6801:16, 6828:25, 6955:18, 6964:18 reaching [2] - 6779:21, 6779:22 react [1] - 6799:8 reaction [1] - 6962:14 reactions [1] - 6962:8 read [5] - 6832:20, 6870:3, 6884:24, 6884:25, 6950:7 reading [1] - 6822:7 real [18] - 6816:9, 6817:23, 6890:18, 6894:7, 6894:10, 6903:7, 6906:20, 6913:8, 6918:11, 6918:19, 6920:12, 6921:3, 6922:5, 6923:4, 6929:5, 6931:14, 6965:4 real-world [4] - 6918:11, 6918:19, 6920:12, 6921:3 realistic [5] - 6826:12, 6893:11, 6910:24, 6956:19, 6964:23 realistically [2] - 6827:8, 6956:16 realities [1] - 6784:22 reality [6] - 6881:3, 6894:1, 6958:22, 6965:3, 6965:4 realize [1] - 6927:18 really [36] - 6788:8, 6789:13, 6796:13, 6798:8, 6802:1, 6802:20, 6803:18, 6817:5, 6819:16, 6820:14, 6821:11, 6826:7, 6828:15, 6829:20, 6831:7, 6832:15, 6843:4, 6844:13, 6850:25, 6858:11, 6859:11, 6862:3, 6871:11, 6875:3, 6886:13, 6907:12, 6907:14, 6927:9, 6937:3, 6940:13, 6941:15, 6942:22, 6952:11, 6955:15, 6960:13 rearview [1] - 6939:5 reason [41] - 6788:23, 6798:24, 6799:10, 6812:13, 6815:4, 6830:11, 6838:10, 6845:16, 6845:22, 6846:11, 6847:10, 6847:12, 6849:6, 6850:3, 6852:20, 6856:23, 6857:8, 6859:7, 6861:17, 6869:4, 6870:9, 6870:15, 6873:2, 6873:25, 6874:4, 6874:15, 6874:23, 6874:25, 6880:10, 6893:3, 6893:12, 6898:5, 6907:1, 6907:19, 6909:10, 6909:19, 6910:12, 6925:12, 6928:2, 6929:24, 6930:16 Reason [2] - 6783:9, 6783:22 reasonable [8] - 6804:14, 6822:13, 6824:6, 6824:8, 6824:24, 6825:18, 6873:14, 6916:2 reasonably [5] - 6804:13, 6824:13, 6879:3, 6879:13, 6915:20 reasons [5] - 6777:3, 6893:10, 6935:11, 6937:6, 6947:16 reassess [1] - 6790:14 rebate [1] - 6814:4 rebuttal [6] - 6776:7, 6777:22, 6872:19, 6884:20, 6932:18, 6949:5 REBUTTAL [1] - 6968:10 recapture [25] - 6796:9, 6839:14, 6839:19, 6840:4, 6840:5, 6842:16,</p>
R		
	<p>rachet [1] - 6959:19 Radio [1] - 6858:4 radiological [1] - 6900:15 raise [6] - 6809:11, 6825:21, 6844:6, 6885:22, 6939:11, 6959:16 raised [8] - 6786:24, 6824:15, 6837:16, 6837:19, 6839:14, 6843:18, 6887:17, 6908:23 raises [3] - 6807:18, 6809:9, 6849:25 raising [4] - 6842:5, 6854:24, 6939:10, 6959:18 ran [1] - 6843:3 range [2] - 6831:13, 6831:17 rarified [1] - 6831:15 rate [13] - 6801:25, 6818:8, 6851:14, 6868:7, 6895:9, 6897:14, 6897:16, 6926:8, 6933:21, 6936:16, 6937:24, 6939:1, 6940:2 rates [52] - 6780:13, 6781:7, 6782:2, 6788:9, 6788:15, 6788:16, 6788:17, 6788:22, 6868:7, 6869:24, 6883:23, 6883:25, 6885:2, 6885:5, 6885:9, 6887:6, 6887:9, 6887:12, 6887:13, 6887:17, 6887:25, 6888:1, 6888:2, 6888:3, 6888:8, 6888:10, 6888:11, 6895:6, 6896:21, 6908:16, 6908:23, 6921:19, 6921:23, 6922:3, 6923:12, 6925:20, 6925:22, 6925:23, 6925:25, 6926:11, 6935:5, 6939:4, 6939:11, 6939:14, 6940:2, 6940:3, 6944:6, 6950:14, 6954:15, 6960:6 rather [5] - 6777:15, 6834:24, 6875:25, 6899:17, 6915:18 rational [2] - 6937:4, 6959:21 rationale [2] - 6868:20, 6925:13 rays [1] - 6952:1</p>	
Q		
<p>qua [1] - 6929:14 Quagliata [2] - 6897:17, 6933:7 qualify [1] - 6863:17 qualitative [1] - 6924:15 quality [8] - 6800:12, 6801:10, 6801:16, 6870:1, 6876:2, 6899:24, 6944:7, 6959:17 quantify [1] - 6839:9</p>		

<p>6842:17, 6844:6, 6844:17, 6846:3, 6850:11, 6850:19, 6851:5, 6851:20, 6853:21, 6854:22, 6855:2, 6937:2, 6937:3, 6937:11, 6937:24, 6938:5, 6938:11, 6938:15, 6940:4</p> <p>Recapture [1] - 6939:12</p> <p>Reccoppa [1] - 6865:9</p> <p>recede [1] - 6945:15</p> <p>recedes [1] - 6935:15</p> <p>receive [2] - 6863:4, 6863:18</p> <p>received [1] - 6891:8</p> <p>receiving [1] - 6921:13</p> <p>recently [3] - 6866:20, 6906:14, 6961:12</p> <p>reception [1] - 6944:20</p> <p>recess [2] - 6864:11, 6949:13</p> <p>Recess [1] - 6822:25</p> <p>recession [4] - 6917:18, 6917:20, 6918:5, 6918:19</p> <p>recites [1] - 6877:2</p> <p>recognize [1] - 6824:4</p> <p>recognized [1] - 6825:2</p> <p>recognizes [2] - 6803:22, 6826:17</p> <p>recollection [1] - 6845:14</p> <p>record [60] - 6776:18, 6776:20, 6789:22, 6791:5, 6791:12, 6791:16, 6793:3, 6794:4, 6794:12, 6794:14, 6798:19, 6798:25, 6812:5, 6813:3, 6816:12, 6816:14, 6817:18, 6821:1, 6829:18, 6830:3, 6839:8, 6842:4, 6846:4, 6847:3, 6847:7, 6847:20, 6849:4, 6867:15, 6870:5, 6870:21, 6887:3, 6888:5, 6888:15, 6888:21, 6891:22, 6892:7, 6892:17, 6893:10, 6895:8, 6896:3, 6898:12, 6904:16, 6908:11, 6910:18, 6911:4, 6912:2, 6921:1, 6921:18, 6922:8, 6925:18, 6929:6, 6934:2, 6938:23, 6939:21, 6942:16, 6956:25, 6957:1, 6957:2</p> <p>recorded [1] - 6772:24</p> <p>recorder [1] - 6909:6</p> <p>records [1] - 6835:5</p> <p>recover [1] - 6812:6</p> <p>recruiting [1] - 6880:22</p> <p>red [5] - 6830:7, 6840:21, 6931:24, 6932:1, 6932:2</p> <p>red-herring [3] - 6931:24, 6932:1, 6932:2</p> <p>redacted [1] - 6829:9</p> <p>redactions [4] - 6777:3, 6840:10, 6840:12</p> <p>redeemed [1] - 6939:8</p> <p>redefine [1] - 6858:19</p> <p>redefined [1] - 6858:13</p> <p>redemptions [1] - 6939:3</p> <p>reduce [5] - 6781:22, 6785:9, 6792:13, 6794:8, 6794:9</p> <p>reducing [3] - 6877:18, 6877:20, 6877:21</p> <p>reduction [1] - 6832:24</p> <p>refer [3] - 6896:14, 6935:1, 6942:16</p> <p>reference [1] - 6922:1</p>	<p>references [3] - 6909:7, 6909:9, 6922:2</p> <p>referred [3] - 6791:12, 6868:15, 6901:9</p> <p>referring [1] - 6881:25</p> <p>reflect [2] - 6793:15, 6953:24</p> <p>reflected [2] - 6840:16, 6904:1</p> <p>reflecting [3] - 6784:21, 6805:16, 6812:8</p> <p>refrigerator [2] - 6813:9, 6814:2</p> <p>refrigerators [1] - 6827:11</p> <p>refuse [1] - 6873:19</p> <p>regard [5] - 6779:7, 6779:11, 6779:16, 6839:22, 6846:7</p> <p>regarding [1] - 6833:8</p> <p>register [2] - 6904:6, 6904:10</p> <p>regression [5] - 6924:17, 6924:19, 6924:24, 6962:8, 6962:10</p> <p>regular [1] - 6803:17</p> <p>regulated [2] - 6888:10, 6961:24</p> <p>regulation [1] - 6962:6</p> <p>regulators [1] - 6831:9</p> <p>regulatory [2] - 6961:13, 6962:1</p> <p>Rein [2] - 6909:18, 6909:19</p> <p>reinstated [1] - 6910:25</p> <p>RELATED [1] - 6772:11</p> <p>related [5] - 6834:17, 6852:4, 6924:12, 6924:13, 6961:25</p> <p>relates [2] - 6834:11, 6962:4</p> <p>relationship [12] - 6817:19, 6838:3, 6846:12, 6846:23, 6846:24, 6848:17, 6849:16, 6849:19, 6889:14, 6907:5, 6923:9, 6937:13</p> <p>relationships [2] - 6790:5, 6937:9</p> <p>relative [1] - 6889:18</p> <p>relatively [1] - 6796:12</p> <p>relevant [35] - 6793:1, 6807:6, 6824:19, 6825:1, 6825:3, 6827:23, 6827:24, 6830:8, 6830:15, 6830:19, 6830:24, 6832:7, 6838:9, 6853:21, 6871:15, 6878:10, 6878:18, 6878:20, 6879:7, 6912:14, 6912:19, 6912:22, 6914:5, 6927:6, 6931:1, 6932:4, 6951:12, 6960:25, 6961:5, 6961:6, 6961:14, 6962:25, 6963:8, 6965:22</p> <p>relief [2] - 6788:24, 6906:11</p> <p>relies [1] - 6916:15</p> <p>rely [4] - 6801:7, 6826:6, 6874:11, 6963:17</p> <p>relying [1] - 6800:24</p> <p>remain [2] - 6900:6, 6900:15</p> <p>remainder [1] - 6776:9</p> <p>remained [1] - 6939:4</p> <p>remains [1] - 6905:8</p> <p>remarkable [5] - 6851:13, 6852:8, 6868:25, 6879:4, 6890:23</p> <p>remedies [3] - 6947:8, 6947:20, 6947:22</p> <p>remedy [13] - 6946:19, 6946:25, 6947:3, 6947:9, 6947:11, 6947:15, 6948:8, 6948:11, 6948:12, 6966:3, 6966:4, 6966:8</p> <p>remember [32] - 6782:18, 6783:15, 6784:11, 6790:25, 6792:10, 6793:20,</p>	<p>6795:18, 6796:4, 6798:3, 6807:8, 6820:24, 6824:2, 6825:17, 6826:17, 6827:10, 6836:10, 6837:9, 6837:20, 6838:15, 6855:2, 6857:23, 6893:19, 6898:11, 6902:19, 6905:17, 6909:17, 6917:15, 6935:16, 6935:25, 6942:18, 6950:22, 6955:3</p> <p>remembering [1] - 6848:17</p> <p>remembers [3] - 6785:4, 6821:16, 6828:11</p> <p>remind [1] - 6940:20</p> <p>reminded [1] - 6824:2</p> <p>reminds [1] - 6955:6</p> <p>remotely [1] - 6803:8</p> <p>remove [2] - 6789:20, 6953:13</p> <p>removed [4] - 6820:18, 6950:23, 6953:7, 6958:6</p> <p>renew [3] - 6848:11, 6936:18, 6936:21</p> <p>renewal [1] - 6936:10</p> <p>rentals [1] - 6829:10</p> <p>reopening [1] - 6779:24</p> <p>repeat [1] - 6783:10</p> <p>repeated [2] - 6875:18, 6899:21</p> <p>repeatedly [2] - 6869:11, 6870:19</p> <p>repeating [3] - 6847:15, 6930:15, 6938:12</p> <p>replace [1] - 6916:23</p> <p>replaced [1] - 6791:7</p> <p>replacement [1] - 6792:9</p> <p>report [4] - 6820:20, 6851:16, 6871:25, 6889:7</p> <p>Reporter [1] - 6772:22</p> <p>reports [2] - 6845:22, 6924:18</p> <p>reposed [1] - 6846:24</p> <p>representative [1] - 6779:18</p> <p>representatives [1] - 6894:1</p> <p>representing [1] - 6839:15</p> <p>require [5] - 6833:14, 6861:22, 6871:7, 6917:22, 6945:6</p> <p>required [4] - 6801:18, 6840:11, 6876:5, 6947:9</p> <p>requirements [1] - 6834:3</p> <p>requires [2] - 6845:24, 6861:12</p> <p>resale [2] - 6873:9, 6873:12</p> <p>reserve [2] - 6776:6, 6776:9</p> <p>Reserve [1] - 6919:8</p> <p>reserving [1] - 6939:7</p> <p>resides [1] - 6874:9</p> <p>resisted [2] - 6922:16, 6922:17</p> <p>resisting [1] - 6956:4</p> <p>resold [1] - 6808:17</p> <p>resolution [1] - 6779:5</p> <p>resolve [1] - 6936:13</p> <p>resolved [5] - 6790:2, 6832:20, 6850:1, 6883:17, 6885:22</p> <p>Resort [1] - 6783:1</p> <p>resources [1] - 6957:5</p> <p>respect [33] - 6843:7, 6862:20, 6866:12, 6869:3, 6869:16, 6871:4, 6871:6, 6872:4, 6878:16, 6881:2, 6883:5, 6885:7, 6895:6, 6897:3, 6912:6,</p>
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<p>6912:23, 6916:12, 6917:3, 6917:10, 6917:11, 6923:16, 6923:24, 6935:20, 6935:23, 6936:19, 6936:20, 6938:11, 6946:11, 6948:12, 6954:24, 6965:12, 6966:18</p> <p>Respectfully [1] - 6919:2</p> <p>respectfully [3] - 6847:1, 6874:21, 6878:15</p> <p>respects [3] - 6866:10, 6898:21, 6903:15</p> <p>respond [6] - 6787:16, 6795:9, 6799:11, 6800:9, 6819:13, 6923:23</p> <p>response [9] - 6786:16, 6786:22, 6795:12, 6809:11, 6809:19, 6821:1, 6825:19, 6859:3, 6885:1</p> <p>responses [2] - 6783:7, 6795:10</p> <p>responsible [1] - 6884:2</p> <p>responsive [1] - 6844:8</p> <p>rest [4] - 6799:14, 6829:12, 6840:22, 6840:23</p> <p>restaurant [1] - 6855:2</p> <p>restaurants [1] - 6926:4</p> <p>rested [1] - 6822:3</p> <p>restored [1] - 6781:13</p> <p>restrain [1] - 6863:8</p> <p>restrains [1] - 6873:4</p> <p>restraint [6] - 6870:12, 6873:5, 6896:8, 6900:6, 6951:15, 6954:24</p> <p>restraints [10] - 6783:3, 6784:1, 6787:10, 6789:20, 6871:6, 6873:3, 6896:15, 6953:8, 6953:14</p> <p>restrict [1] - 6862:22</p> <p>restricted [1] - 6787:21</p> <p>restriction [14] - 6803:3, 6806:2, 6808:8, 6808:10, 6859:7, 6860:1, 6860:2, 6860:6, 6950:21, 6950:23, 6950:25, 6951:2, 6960:9</p> <p>restrictions [3] - 6856:6, 6861:14, 6863:6</p> <p>rests [1] - 6880:11</p> <p>result [15] - 6780:15, 6780:17, 6784:8, 6787:9, 6789:19, 6789:22, 6789:24, 6798:17, 6799:17, 6825:15, 6840:17, 6852:9, 6906:18, 6906:25, 6945:6</p> <p>resulted [1] - 6951:20</p> <p>results [3] - 6883:13, 6883:16, 6950:11</p> <p>resume [2] - 6822:24, 6864:9</p> <p>retail [1] - 6812:19</p> <p>retailer [2] - 6873:10, 6904:10</p> <p>retailers [1] - 6786:9</p> <p>retain [2] - 6781:20, 6862:6</p> <p>retaliating [1] - 6850:4</p> <p>retaliation [2] - 6845:13, 6846:20</p> <p>retire [1] - 6821:4</p> <p>return [4] - 6818:16, 6926:12, 6935:8, 6935:11</p> <p>revealed [1] - 6962:17</p> <p>revenue [10] - 6816:17, 6816:20, 6851:14, 6852:3, 6852:6, 6852:7, 6852:17, 6852:18, 6855:8</p> <p>revenues [1] - 6828:23</p>	<p>reverse [3] - 6817:21, 6844:16, 6940:1</p> <p>reversed [2] - 6909:19, 6910:9</p> <p>revolutionary [1] - 6803:18</p> <p>revolvers [1] - 6914:18</p> <p>revolving [3] - 6914:4, 6914:11, 6915:14</p> <p>reward [15] - 6784:7, 6791:23, 6793:16, 6813:12, 6815:10, 6816:18, 6818:9, 6820:6, 6820:7, 6841:22, 6841:25, 6845:18, 6959:25</p> <p>rewarded [2] - 6791:22, 6794:7</p> <p>rewards [37] - 6810:12, 6812:10, 6812:11, 6812:16, 6813:17, 6814:19, 6832:16, 6841:14, 6841:16, 6841:17, 6842:6, 6842:9, 6843:17, 6844:1, 6844:7, 6845:9, 6846:1, 6860:25, 6861:9, 6863:19, 6880:20, 6880:21, 6888:13, 6889:15, 6898:17, 6939:3, 6939:8, 6941:13, 6945:13, 6945:14, 6945:15, 6953:17, 6959:1, 6960:5</p> <p>rid [5] - 6862:2, 6862:10, 6885:9, 6951:1, 6959:24</p> <p>riding [5] - 6911:13, 6911:14, 6911:23, 6912:1, 6912:3</p> <p>rise [2] - 6774:3, 6823:3</p> <p>risk [3] - 6894:7, 6894:10</p> <p>rivals [7] - 6810:17, 6819:2, 6858:16, 6859:2, 6860:13, 6861:11, 6861:25</p> <p>road [3] - 6876:18, 6893:15, 6940:17</p> <p>roadmap [6] - 6838:19, 6838:20, 6838:22, 6839:12, 6839:18, 6853:22</p> <p>Robinson [2] - 6784:15, 6856:24</p> <p>rocketing [1] - 6954:14</p> <p>rocky [1] - 6798:16</p> <p>role [2] - 6836:12, 6867:7</p> <p>roll [1] - 6793:13</p> <p>rolled [1] - 6841:9</p> <p>roof [1] - 6939:4</p> <p>room [2] - 6789:4, 6806:18</p> <p>roulette [1] - 6907:23</p> <p>round [1] - 6774:10</p> <p>rounding [1] - 6910:9</p> <p>route [1] - 6930:1</p> <p>rudimentary [1] - 6875:11</p> <p>Rule [2] - 6783:9, 6783:22</p> <p>rule [11] - 6793:24, 6810:25, 6811:17, 6814:15, 6870:9, 6870:15, 6873:25, 6874:4, 6874:15, 6874:23, 6874:24</p> <p>ruled [1] - 6821:18</p> <p>Rules [1] - 6901:25</p> <p>RULES [1] - 6772:15</p> <p>rules [64] - 6781:19, 6782:3, 6783:13, 6783:18, 6784:5, 6784:9, 6785:6, 6785:10, 6785:12, 6786:20, 6789:22, 6789:25, 6790:19, 6791:24, 6792:18, 6792:22, 6793:10, 6793:18, 6794:5, 6794:18, 6795:13, 6795:23, 6800:18, 6800:20, 6811:25, 6812:2, 6812:5, 6815:5, 6815:14, 6815:23, 6816:15, 6821:10, 6822:18, 6856:11, 6857:25, 6859:4, 6859:10, 6861:3, 6862:3,</p>	<p>6862:6, 6862:10, 6862:12, 6862:22, 6862:25, 6864:3, 6867:5, 6877:8, 6877:17, 6887:11, 6887:14, 6887:20, 6887:23, 6888:7, 6903:4, 6903:6, 6903:7, 6911:15, 6928:17, 6950:11, 6952:16, 6957:10, 6958:6, 6959:17</p> <p>ruling [1] - 6801:11</p> <p>run [7] - 6791:2, 6842:20, 6851:23, 6893:15, 6935:20, 6935:21, 6965:16</p> <p>run-up [1] - 6851:23</p> <p>running [2] - 6836:9, 6890:7</p> <p>runs [1] - 6902:20</p> <p>rushed [2] - 6842:25, 6843:3</p> <p>RYAN [2] - 6773:7, 6774:16</p> <p>Ryan [1] - 6774:16</p>
S		
<p>Safeway [5] - 6904:21, 6904:22, 6935:25, 6936:2, 6936:5</p> <p>sake [1] - 6946:18</p> <p>salaries [2] - 6876:8, 6876:16</p> <p>sale [11] - 6781:4, 6784:10, 6786:10, 6858:16, 6858:17, 6889:14, 6904:25, 6906:23, 6906:25, 6915:8, 6961:4</p> <p>sales [6] - 6780:15, 6781:12, 6781:13, 6784:8, 6827:14, 6911:21</p> <p>salesmanship [1] - 6839:7</p> <p>San [3] - 6831:16, 6933:14, 6965:17</p> <p>Sandwiches [1] - 6928:11</p> <p>sandwiching [1] - 6919:25</p> <p>sanity [2] - 6930:6, 6930:11</p> <p>sat [2] - 6890:9, 6937:7</p> <p>satisfied [1] - 6945:19</p> <p>save [1] - 6948:1</p> <p>saving [2] - 6872:18, 6889:1</p> <p>savings [2] - 6883:24, 6883:25</p> <p>saw [14] - 6788:15, 6809:4, 6843:6, 6884:7, 6889:5, 6889:7, 6906:7, 6906:10, 6945:16, 6945:17, 6952:24, 6952:25, 6957:4</p> <p>scale [1] - 6894:9</p> <p>scared [1] - 6902:7</p> <p>scenario [1] - 6888:18</p> <p>scenarios [1] - 6894:12</p> <p>schedules [2] - 6925:20</p> <p>SCHILLER [1] - 6773:15</p> <p>School [3] - 6886:7, 6886:9, 6886:21</p> <p>Schulman [1] - 6866:21</p> <p>screen [3] - 6895:2, 6921:25, 6923:18</p> <p>screwed [1] - 6936:3</p> <p>se [3] - 6874:4, 6874:7, 6875:15</p> <p>searching [1] - 6874:14</p> <p>Sears [3] - 6813:9, 6827:10, 6909:14</p> <p>seated [3] - 6774:4, 6823:4, 6949:15</p> <p>SEC [1] - 6934:18</p> <p>second [15] - 6783:21, 6829:16, 6859:24, 6914:1, 6921:9, 6921:11, 6926:9, 6934:10, 6951:6, 6951:17, 6955:12, 6956:1, 6956:9, 6959:5, 6959:9</p>		

<p>Second [15] - 6869:10, 6870:4, 6870:10, 6870:15, 6871:19, 6873:12, 6875:19, 6875:21, 6882:22, 6899:20, 6900:11, 6912:15, 6932:16, 6932:20, 6941:11</p> <p>secret [1] - 6912:25</p> <p>section [2] - 6866:1, 6966:15</p> <p>Section [9] - 6783:9, 6811:12, 6862:13, 6864:1, 6868:18, 6870:3, 6870:8, 6870:9, 6947:2</p> <p>sections [1] - 6876:19</p> <p>sector [2] - 6831:3, 6855:11</p> <p>sectors [1] - 6831:6</p> <p>security [1] - 6919:10</p> <p>sedatives [1] - 6891:10</p> <p>see [53] - 6786:14, 6787:1, 6787:4, 6787:6, 6789:7, 6793:1, 6794:15, 6797:14, 6805:2, 6805:4, 6805:7, 6805:14, 6806:15, 6807:12, 6817:9, 6820:3, 6825:23, 6825:25, 6826:2, 6828:25, 6829:13, 6833:4, 6840:5, 6840:18, 6841:4, 6851:17, 6851:19, 6853:9, 6853:10, 6853:17, 6853:19, 6861:1, 6862:14, 6865:22, 6866:11, 6877:16, 6883:16, 6883:20, 6884:15, 6884:16, 6905:12, 6916:7, 6918:21, 6923:19, 6924:7, 6924:22, 6937:22, 6941:16, 6941:17, 6960:1, 6962:14, 6965:5</p> <p>seeing [1] - 6869:15</p> <p>seem [1] - 6869:18</p> <p>sees [1] - 6786:15</p> <p>selection [1] - 6863:5</p> <p>self [2] - 6790:12, 6933:7</p> <p>self-correction [1] - 6790:12</p> <p>self-inflicted [1] - 6933:7</p> <p>sell [8] - 6807:13, 6827:11, 6831:25, 6849:10, 6873:10, 6873:19, 6873:20, 6918:17</p> <p>seller [1] - 6945:1</p> <p>sellers [1] - 6831:22</p> <p>selling [4] - 6805:13, 6805:25, 6806:1, 6885:11</p> <p>sells [1] - 6807:25</p> <p>senators [1] - 6908:2</p> <p>send [1] - 6837:14</p> <p>senior [2] - 6779:18, 6866:21</p> <p>sense [15] - 6789:10, 6790:18, 6849:23, 6852:16, 6874:6, 6915:8, 6926:7, 6927:4, 6927:10, 6928:9, 6928:19, 6929:7, 6942:14, 6947:18, 6964:20</p> <p>sensitive [1] - 6905:8</p> <p>sent [2] - 6936:11, 6948:11</p> <p>sentence [2] - 6866:7, 6877:25</p> <p>sentences [2] - 6912:18, 6946:20</p> <p>separate [19] - 6791:3, 6803:23, 6805:2, 6807:9, 6837:15, 6858:4, 6871:22, 6876:20, 6893:24, 6897:17, 6899:4, 6921:12, 6925:24, 6930:13, 6930:14, 6948:7, 6948:11, 6964:12, 6966:5</p> <p>series [3] - 6842:8, 6860:14, 6913:22</p> <p>serious [1] - 6909:8</p>	<p>seriously [1] - 6858:9</p> <p>Servers [1] - 6932:19</p> <p>service [3] - 6878:12, 6899:23, 6960:5</p> <p>services [18] - 6798:7, 6805:13, 6805:25, 6806:2, 6806:4, 6806:5, 6806:8, 6807:9, 6808:16, 6808:18, 6827:22, 6863:18, 6877:23, 6878:20, 6900:15, 6951:21, 6958:8, 6963:9</p> <p>Services [2] - 6829:3, 6829:12</p> <p>SERVICES [1] - 6772:11</p> <p>serving [1] - 6830:19</p> <p>SESSION [1] - 6865:1</p> <p>session [1] - 6793:25</p> <p>set [12] - 6777:5, 6792:16, 6796:6, 6797:24, 6806:5, 6820:5, 6834:9, 6840:20, 6840:25, 6848:8, 6908:1, 6928:17</p> <p>Seth [1] - 6774:13</p> <p>SETH [1] - 6773:6</p> <p>setting [9] - 6781:14, 6784:2, 6784:5, 6808:9, 6808:10, 6848:14, 6872:10, 6951:19, 6952:2</p> <p>settleable [1] - 6779:13</p> <p>settled [1] - 6779:13</p> <p>settlement [5] - 6779:20, 6807:11, 6883:12, 6883:21, 6942:8</p> <p>settlements [1] - 6891:18</p> <p>settling [1] - 6790:13</p> <p>seven [4] - 6899:19, 6903:9, 6910:21, 6936:8</p> <p>seventeen [1] - 6864:4</p> <p>seventy [2] - 6835:5, 6898:2</p> <p>several [6] - 6852:10, 6862:20, 6875:22, 6877:7, 6886:20, 6922:15</p> <p>Several [1] - 6899:2</p> <p>shape [1] - 6810:21</p> <p>share [39] - 6791:13, 6796:12, 6797:2, 6798:23, 6799:2, 6799:5, 6820:2, 6853:24, 6854:3, 6854:5, 6854:6, 6867:20, 6867:21, 6868:9, 6892:12, 6892:18, 6910:19, 6913:1, 6913:4, 6918:14, 6918:15, 6918:18, 6923:22, 6925:11, 6930:17, 6930:18, 6931:16, 6931:20, 6932:6, 6932:17, 6934:5, 6941:16, 6955:2, 6956:20, 6958:2</p> <p>shareholder [2] - 6818:2, 6818:17</p> <p>shareholders [1] - 6893:24</p> <p>shares [3] - 6795:7, 6907:20, 6933:1</p> <p>shattered [1] - 6821:20</p> <p>shaving [2] - 6927:19, 6927:20</p> <p>sheet [1] - 6865:13</p> <p>Sherman [7] - 6808:2, 6810:4, 6864:2, 6868:18, 6871:5, 6947:2, 6966:16</p> <p>shift [3] - 6781:3, 6797:2, 6824:19</p> <p>shifted [1] - 6795:8</p> <p>Shoe [1] - 6824:3</p> <p>shop [1] - 6942:17</p> <p>shopping [1] - 6919:24</p> <p>short [6] - 6779:6, 6821:8, 6822:20, 6842:20, 6947:1, 6947:2</p> <p>shortcut [1] - 6930:1</p>	<p>show [9] - 6872:9, 6873:1, 6882:10, 6900:19, 6901:8, 6905:7, 6922:5, 6927:1, 6936:1</p> <p>showed [13] - 6820:21, 6835:21, 6900:5, 6903:21, 6907:12, 6919:21, 6919:24, 6920:3, 6920:16, 6921:5, 6921:11, 6923:6, 6927:25</p> <p>showing [8] - 6837:6, 6878:23, 6882:13, 6900:17, 6918:3, 6936:23, 6936:25</p> <p>shown [5] - 6801:2, 6862:22, 6900:21, 6900:23, 6961:1</p> <p>shows [25] - 6780:10, 6787:2, 6791:18, 6793:4, 6795:17, 6804:22, 6808:15, 6811:24, 6813:3, 6816:14, 6817:23, 6839:8, 6853:20, 6855:7, 6905:25, 6906:14, 6911:16, 6921:1, 6921:18, 6922:8, 6931:1, 6938:23, 6938:25, 6939:21, 6945:25</p> <p>shred [1] - 6885:24</p> <p>shrink [1] - 6918:5</p> <p>shrinking [2] - 6871:12, 6912:10</p> <p>shut [1] - 6795:13</p> <p>side [48] - 6796:1, 6801:25, 6802:16, 6803:5, 6803:9, 6803:10, 6804:1, 6808:25, 6812:3, 6814:18, 6815:3, 6817:6, 6834:12, 6838:10, 6852:4, 6863:9, 6869:21, 6871:21, 6871:22, 6879:20, 6881:5, 6881:18, 6881:23, 6882:4, 6882:8, 6882:10, 6887:15, 6887:19, 6894:8, 6894:9, 6897:25, 6898:20, 6902:20, 6917:10, 6917:11, 6918:23, 6919:5, 6919:7, 6921:2, 6922:5, 6923:11, 6923:14, 6923:15, 6932:11, 6951:1, 6951:2, 6963:1</p> <p>sided [21] - 6801:24, 6803:9, 6803:11, 6803:16, 6803:22, 6804:7, 6807:24, 6816:9, 6817:12, 6861:1, 6869:13, 6869:15, 6869:18, 6871:24, 6872:1, 6872:3, 6878:12, 6882:4, 6885:11, 6887:15, 6895:10</p> <p>sidedly [1] - 6844:5</p> <p>sidedness [4] - 6802:20, 6807:20, 6820:13, 6823:22</p> <p>sides [9] - 6779:7, 6779:23, 6802:3, 6802:4, 6817:6, 6888:14, 6897:25, 6919:4, 6966:7</p> <p>sign [7] - 6836:13, 6836:18, 6858:1, 6858:22, 6890:17, 6898:8, 6933:23</p> <p>signage [1] - 6904:3</p> <p>significant [6] - 6782:18, 6916:17, 6917:1, 6917:19, 6918:14, 6961:14</p> <p>significantly [1] - 6964:24</p> <p>signing [3] - 6933:25, 6936:5, 6963:1</p> <p>signs [5] - 6785:4, 6795:4, 6799:23, 6857:23, 6937:20</p> <p>Silverman [3] - 6902:18, 6933:12, 6935:3</p> <p>similar [3] - 6781:23, 6924:1, 6951:3</p> <p>similarly [1] - 6820:9</p> <p>simple [4] - 6786:8, 6817:19, 6858:16, 6889:20</p>
---	--	--

<p>simple-priced [1] - 6786:8</p> <p>simpler [2] - 6861:12, 6887:1</p> <p>simply [10] - 6871:4, 6871:8, 6878:7, 6887:2, 6888:15, 6922:6, 6929:10, 6933:17, 6934:1, 6941:21</p> <p>Sinclair [2] - 6793:11, 6793:12</p> <p>single [13] - 6788:21, 6805:5, 6833:7, 6870:5, 6870:9, 6870:11, 6871:23, 6893:21, 6910:20, 6913:3, 6942:6, 6944:19, 6952:14</p> <p>sit [1] - 6945:4</p> <p>site [1] - 6793:22</p> <p>sites [1] - 6875:17</p> <p>sitting [4] - 6908:25, 6928:24, 6933:19, 6934:1</p> <p>situated [1] - 6820:9</p> <p>situation [4] - 6777:14, 6788:7, 6831:12, 6846:7</p> <p>situations [2] - 6894:13, 6922:2</p> <p>six [13] - 6778:16, 6778:18, 6778:24, 6797:19, 6854:3, 6854:4, 6854:6, 6881:22, 6891:2, 6923:15, 6941:1, 6952:4, 6958:3</p> <p>six-week [3] - 6778:16, 6778:24, 6952:4</p> <p>sixty [1] - 6839:15</p> <p>sixty-five [1] - 6839:15</p> <p>size [4] - 6884:13, 6910:20, 6919:25, 6943:3</p> <p>Ski [1] - 6783:1</p> <p>skip [2] - 6827:2, 6854:9</p> <p>Sky [5] - 6843:9, 6843:10, 6843:13, 6843:18, 6843:20</p> <p>skyrocketing [1] - 6939:4</p> <p>slapped [1] - 6888:11</p> <p>sleepless [1] - 6909:20</p> <p>sleeves [1] - 6891:18</p> <p>slide [53] - 6787:1, 6787:2, 6787:6, 6793:2, 6794:21, 6800:3, 6804:20, 6806:15, 6806:16, 6806:19, 6806:24, 6823:20, 6828:17, 6829:9, 6831:12, 6838:15, 6838:16, 6840:2, 6851:3, 6851:15, 6851:16, 6854:12, 6855:6, 6856:14, 6856:15, 6865:5, 6865:10, 6875:5, 6875:19, 6877:10, 6881:22, 6895:1, 6899:19, 6900:11, 6901:10, 6903:24, 6905:9, 6905:18, 6906:13, 6906:22, 6912:15, 6914:1, 6918:1, 6918:3, 6919:15, 6923:19, 6924:1, 6930:20, 6931:3, 6931:7, 6931:12</p> <p>slides [10] - 6776:16, 6776:25, 6777:1, 6804:17, 6854:10, 6865:20, 6913:20, 6919:21, 6921:24, 6966:18</p> <p>slightly [1] - 6964:19</p> <p>slope [2] - 6894:23, 6895:12</p> <p>slopes [1] - 6783:2</p> <p>slowed [1] - 6940:2</p> <p>slowly [1] - 6799:1</p> <p>small [13] - 6791:14, 6825:20, 6836:8, 6839:16, 6840:9, 6884:4, 6891:24, 6941:22, 6942:1, 6942:15, 6943:2, 6962:7, 6962:14</p>	<p>smaller [3] - 6884:12, 6933:5, 6933:6</p> <p>smallest [1] - 6903:11</p> <p>smarter [2] - 6885:17, 6918:6</p> <p>snack [1] - 6927:23</p> <p>snowballing [1] - 6905:6</p> <p>SNYDER [1] - 6773:5</p> <p>soaring [1] - 6923:13</p> <p>Society [1] - 6858:24</p> <p>society [1] - 6880:7</p> <p>softer [1] - 6822:17</p> <p>software [1] - 6816:9</p> <p>sold [5] - 6806:4, 6806:5, 6808:16, 6808:18, 6873:22</p> <p>solely [1] - 6882:4</p> <p>solicit [1] - 6834:23</p> <p>Solitude [1] - 6782:25</p> <p>solution [3] - 6833:1, 6948:23, 6959:24</p> <p>solve [3] - 6827:6, 6833:4, 6929:10</p> <p>someone [4] - 6791:25, 6960:22, 6963:2, 6965:12</p> <p>sometime [1] - 6965:13</p> <p>sometimes [5] - 6775:21, 6805:22, 6813:5, 6964:14</p> <p>somewhat [1] - 6958:11</p> <p>soon [4] - 6884:4, 6884:5, 6884:10, 6884:11</p> <p>sophisticated [1] - 6938:19</p> <p>sorry [4] - 6808:11, 6833:19, 6840:8, 6910:25</p> <p>sort [8] - 6782:9, 6790:10, 6797:22, 6814:22, 6910:3, 6946:19, 6947:3, 6947:13</p> <p>sorts [1] - 6933:22</p> <p>Sotomayor [1] - 6876:4</p> <p>Sotomayor's [1] - 6876:14</p> <p>sought [1] - 6867:13</p> <p>source [1] - 6905:1</p> <p>Southwest [3] - 6780:8, 6781:23, 6792:11</p> <p>space [11] - 6792:14, 6832:1, 6832:3, 6832:9, 6832:12, 6836:16, 6846:7, 6846:9, 6848:6, 6848:7, 6848:12</p> <p>speaking [3] - 6776:4, 6918:2, 6937:14</p> <p>special [6] - 6810:8, 6810:19, 6837:13, 6854:24, 6858:7, 6965:5</p> <p>specific [2] - 6828:22, 6922:2</p> <p>specifically [4] - 6790:23, 6827:18, 6842:7, 6901:9</p> <p>specifics [1] - 6842:14</p> <p>speculation [5] - 6868:24, 6868:25, 6870:21, 6907:17, 6929:5</p> <p>speech [5] - 6798:24, 6798:25, 6893:22, 6901:23, 6902:4</p> <p>spend [36] - 6783:1, 6797:23, 6799:12, 6800:19, 6826:18, 6854:16, 6866:14, 6867:21, 6868:9, 6868:10, 6893:1, 6901:1, 6901:6, 6901:7, 6904:19, 6908:14, 6909:12, 6909:18, 6910:5, 6910:19, 6910:23, 6920:14, 6920:15, 6920:24, 6921:6, 6922:6, 6923:13, 6925:23, 6927:20, 6940:15, 6941:16, 6957:7, 6963:24, 6965:12</p>	<p>Spend [1] - 6904:10</p> <p>spending [3] - 6799:21, 6851:9, 6904:22</p> <p>spent [9] - 6835:5, 6864:5, 6869:21, 6880:16, 6902:15, 6919:17, 6929:12, 6938:12, 6947:7</p> <p>spill [4] - 6965:11, 6965:14, 6965:16, 6965:18</p> <p>spill-over [4] - 6965:11, 6965:14, 6965:16, 6965:18</p> <p>spilling [1] - 6903:23</p> <p>spilling-over [1] - 6903:23</p> <p>spillover [9] - 6904:23, 6905:3, 6905:8, 6905:11, 6906:17, 6927:9, 6928:19, 6928:21, 6929:5</p> <p>spin [1] - 6957:16</p> <p>spinning [1] - 6832:21</p> <p>spins [1] - 6833:3</p> <p>spiraling [1] - 6905:6</p> <p>spite [1] - 6839:21</p> <p>spread [1] - 6818:1</p> <p>spun [1] - 6796:7</p> <p>square [1] - 6954:16</p> <p>squelched [4] - 6801:19, 6861:2, 6861:3, 6861:4</p> <p>SSNIP [7] - 6924:6, 6924:11, 6924:14, 6924:16, 6926:17, 6927:1</p> <p>staff [2] - 6778:14, 6967:3</p> <p>stand [11] - 6810:15, 6867:4, 6880:6, 6884:20, 6889:6, 6903:14, 6909:14, 6910:25, 6914:2, 6942:11, 6945:24</p> <p>standalone [1] - 6889:18</p> <p>standard [32] - 6800:23, 6801:21, 6807:22, 6811:12, 6811:24, 6824:6, 6824:23, 6869:11, 6870:13, 6870:14, 6871:1, 6871:3, 6872:25, 6873:8, 6873:16, 6874:1, 6874:2, 6874:22, 6874:25, 6875:8, 6875:17, 6875:18, 6876:5, 6877:2, 6878:2, 6914:7, 6916:20, 6934:23, 6945:20, 6945:21, 6952:21, 6965:1</p> <p>standards [2] - 6869:8, 6874:3</p> <p>standing [6] - 6890:4, 6890:8, 6904:6, 6904:9, 6944:17, 6959:24</p> <p>standpoint [1] - 6955:25</p> <p>stands [4] - 6803:6, 6803:7, 6899:7, 6951:11</p> <p>star [1] - 6901:24</p> <p>start [5] - 6778:13, 6825:11, 6913:19, 6916:13, 6918:9</p> <p>starting [1] - 6919:2</p> <p>starts [1] - 6906:2</p> <p>Starwood [1] - 6915:2</p> <p>STATE [7] - 6772:4, 6772:4, 6772:5, 6772:5, 6772:6, 6772:6, 6772:7</p> <p>State [2] - 6773:9, 6904:19</p> <p>state [1] - 6774:6</p> <p>statement [12] - 6821:25, 6847:15, 6876:20, 6877:14, 6879:4, 6882:5, 6882:6, 6882:17, 6883:10, 6890:14,</p>
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<p>6890:23, 6924:1</p> <p>statements [4] - 6821:20, 6821:22, 6860:14, 6875:24</p> <p>states [2] - 6899:21, 6966:24</p> <p>STATES [2] - 6772:1, 6772:3</p> <p>States [27] - 6772:20, 6774:8, 6774:11, 6774:13, 6774:14, 6774:15, 6774:16, 6774:19, 6774:20, 6774:24, 6782:19, 6799:21, 6821:18, 6860:15, 6862:19, 6863:13, 6863:23, 6864:5, 6867:6, 6868:16, 6872:20, 6880:8, 6883:19, 6888:17, 6889:23, 6892:17</p> <p>stay [4] - 6913:7, 6935:7, 6936:10, 6944:21</p> <p>staying [1] - 6851:11</p> <p>steer [21] - 6781:10, 6781:24, 6784:13, 6784:18, 6784:19, 6784:25, 6787:24, 6788:1, 6794:8, 6814:10, 6815:6, 6836:14, 6836:22, 6837:13, 6856:21, 6862:23, 6885:21, 6891:15, 6891:16, 6891:19, 6892:1</p> <p>steered [2] - 6792:20, 6911:22</p> <p>steering [65] - 6781:9, 6781:17, 6781:19, 6782:2, 6782:4, 6783:13, 6783:18, 6784:9, 6784:10, 6784:11, 6785:3, 6785:5, 6785:8, 6786:10, 6786:11, 6786:20, 6790:19, 6791:24, 6792:18, 6792:22, 6793:10, 6793:18, 6793:24, 6795:13, 6811:25, 6812:2, 6812:5, 6813:5, 6813:10, 6815:5, 6815:9, 6815:14, 6815:21, 6815:23, 6816:14, 6820:18, 6821:10, 6836:12, 6837:9, 6837:17, 6837:22, 6856:17, 6856:20, 6856:22, 6857:25, 6858:10, 6861:3, 6862:3, 6862:5, 6862:10, 6862:12, 6862:22, 6864:3, 6884:7, 6884:11, 6885:20, 6891:20, 6892:4, 6896:18, 6910:16, 6912:1, 6912:3, 6945:13, 6952:16, 6957:10</p> <p>STEERING [1] - 6772:15</p> <p>steers [3] - 6784:15, 6857:10, 6857:12</p> <p>stenography [1] - 6772:24</p> <p>step [6] - 6783:8, 6783:11, 6912:19, 6948:16, 6948:25</p> <p>step-by-step [1] - 6783:11</p> <p>stepping [1] - 6951:23</p> <p>Stern [1] - 6886:21</p> <p>stick [3] - 6817:13, 6825:22, 6929:3</p> <p>sticking [1] - 6892:21</p> <p>still [10] - 6839:23, 6841:9, 6861:3, 6870:8, 6874:8, 6880:7, 6893:18, 6905:11, 6935:5, 6962:18</p> <p>stock [3] - 6818:6, 6890:4, 6890:10</p> <p>stood [2] - 6878:21, 6890:9</p> <p>stop [18] - 6795:14, 6795:23, 6806:3, 6826:6, 6880:22, 6880:24, 6881:13, 6893:2, 6898:7, 6899:13, 6906:13, 6927:19, 6928:10, 6936:12, 6937:5, 6941:14, 6945:12</p> <p>stopped [4] - 6800:10, 6826:10, 6937:6, 6940:4</p>	<p>store [7] - 6881:8, 6904:3, 6904:22, 6920:15, 6920:19, 6942:24, 6944:19</p> <p>stores [4] - 6791:3, 6904:22, 6919:25, 6920:12</p> <p>stories [1] - 6940:9</p> <p>story [2] - 6909:25, 6940:8</p> <p>stoves [1] - 6827:11</p> <p>straightforward [1] - 6876:21</p> <p>strains [1] - 6933:17</p> <p>strategy [21] - 6780:20, 6780:23, 6781:2, 6786:11, 6786:12, 6786:19, 6787:25, 6789:6, 6795:1, 6797:4, 6802:3, 6802:4, 6889:6, 6889:20, 6906:18, 6908:6, 6908:16, 6917:18, 6925:8, 6959:21, 6963:16</p> <p>streamline [1] - 6823:17</p> <p>street [3] - 6911:7, 6927:24, 6963:25</p> <p>Street [2] - 6773:3, 6883:14</p> <p>strengths [1] - 6778:25</p> <p>strenuously [1] - 6950:10</p> <p>Strictly [1] - 6942:17</p> <p>strong [4] - 6797:6, 6797:7, 6797:21, 6835:4</p> <p>stronger [6] - 6797:22, 6854:18, 6855:4, 6855:11, 6891:9, 6952:9</p> <p>structure [4] - 6788:4, 6796:8, 6797:14, 6797:16</p> <p>structured [1] - 6936:4</p> <p>stuck [1] - 6944:20</p> <p>studies [1] - 6905:7</p> <p>Studios [1] - 6857:18</p> <p>study [2] - 6905:20, 6905:25</p> <p>stuff [1] - 6889:24</p> <p>stunning [1] - 6946:8</p> <p>Stunting [1] - 6877:10</p> <p>stunting [2] - 6877:13, 6877:24</p> <p>subject [10] - 6779:25, 6782:3, 6825:16, 6868:4, 6872:22, 6883:7, 6886:22, 6887:4, 6955:6, 6966:8</p> <p>submarket [6] - 6797:8, 6827:20, 6827:23, 6838:7, 6964:10, 6964:23</p> <p>submission [1] - 6926:14</p> <p>submit [16] - 6868:12, 6870:24, 6873:2, 6874:21, 6878:7, 6893:3, 6893:8, 6893:11, 6896:2, 6903:18, 6936:22, 6940:7, 6945:2, 6945:22, 6950:18, 6966:6</p> <p>subsequent [1] - 6840:19</p> <p>substance [1] - 6950:2</p> <p>substantial [9] - 6807:11, 6826:15, 6835:23, 6841:8, 6851:23, 6876:7, 6876:15, 6932:22, 6936:23</p> <p>substantively [1] - 6948:2</p> <p>substitute [8] - 6806:8, 6807:3, 6827:16, 6879:2, 6913:24, 6914:9, 6915:8, 6964:7</p> <p>substitutes [7] - 6826:8, 6913:13, 6914:12, 6914:20, 6915:19, 6915:20</p> <p>substitution [1] - 6916:12</p> <p>subtracting [1] - 6960:14</p> <p>Subway [1] - 6928:11</p>	<p>succeed [8] - 6787:11, 6800:2, 6860:12, 6861:24, 6952:16, 6957:11, 6958:7, 6960:1</p> <p>succeeded [1] - 6799:15</p> <p>success [6] - 6860:13, 6901:13, 6901:18, 6905:15, 6957:14, 6960:20</p> <p>successful [8] - 6798:8, 6799:19, 6839:23, 6841:10, 6841:12, 6844:20, 6867:23, 6960:19</p> <p>successfully [1] - 6799:18</p> <p>sue [3] - 6892:12, 6907:20, 6909:11</p> <p>sued [9] - 6779:12, 6796:4, 6807:10, 6854:5, 6888:1, 6888:2, 6888:3, 6892:14, 6945:23</p> <p>suffering [1] - 6880:18</p> <p>sufficient [4] - 6875:25, 6951:14, 6952:18, 6953:24</p> <p>suggest [7] - 6849:4, 6879:8, 6880:17, 6884:1, 6885:6, 6905:13, 6933:18</p> <p>suggested [6] - 6869:14, 6882:16, 6896:2, 6914:10, 6934:24, 6939:12</p> <p>suggesting [9] - 6811:3, 6859:6, 6878:3, 6880:2, 6886:16, 6886:24, 6896:21, 6896:24, 6966:6</p> <p>suggestion [7] - 6820:17, 6852:25, 6885:8, 6888:19, 6895:8, 6935:2, 6935:19</p> <p>suggestions [1] - 6909:7</p> <p>suggests [6] - 6890:21, 6902:12, 6920:19, 6930:18, 6944:15, 6965:22</p> <p>suing [1] - 6930:16</p> <p>Suite [1] - 6773:3</p> <p>suits [3] - 6879:7, 6879:16</p> <p>sum [2] - 6800:3, 6840:3</p> <p>sum-up [1] - 6840:3</p> <p>summarize [2] - 6824:9, 6841:1</p> <p>summary [4] - 6869:17, 6872:2, 6912:18, 6929:19</p> <p>SUMMATION [3] - 6778:9, 6968:6, 6968:8</p> <p>sums [2] - 6780:9, 6829:20</p> <p>super [2] - 6934:8, 6953:15</p> <p>supermarket [2] - 6798:13, 6889:25</p> <p>supplied [1] - 6887:7</p> <p>supplier [1] - 6905:3</p> <p>supply [2] - 6965:9, 6965:23</p> <p>support [10] - 6820:22, 6821:5, 6845:12, 6850:5, 6876:7, 6876:15, 6895:8, 6896:3, 6911:4, 6951:14</p> <p>supported [6] - 6798:18, 6817:17, 6839:25, 6846:3, 6890:22, 6913:11</p> <p>supports [1] - 6816:7</p> <p>suppose [3] - 6847:4, 6879:7, 6913:22</p> <p>supposed [3] - 6916:18, 6929:20, 6929:22</p> <p>suppressed [1] - 6952:13</p> <p>suppression [2] - 6839:17, 6950:4</p> <p>supra [1] - 6896:23</p> <p>supra-competitive [1] - 6896:23</p> <p>Supreme [11] - 6783:25, 6785:15, 6801:1, 6824:2, 6858:23, 6874:10,</p>
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<p>6875:7, 6875:16, 6876:3, 6951:10, 6952:7</p> <p>surely [1] - 6884:1</p> <p>surmise [2] - 6821:23, 6846:18</p> <p>surprise [2] - 6856:20, 6964:12</p> <p>surprised [2] - 6866:8, 6942:1</p> <p>surprising [1] - 6859:17</p> <p>surprisingly [1] - 6879:18</p> <p>survey [2] - 6919:9, 6919:12</p> <p>survive [4] - 6796:14, 6799:13, 6902:16, 6911:25</p> <p>survived [3] - 6796:10, 6796:20, 6799:22</p> <p>surviving [1] - 6799:7</p> <p>suspect [2] - 6828:11, 6920:10</p> <p>sustain [9] - 6830:6, 6830:9, 6830:11, 6830:18, 6830:19, 6833:6, 6925:24, 6960:15, 6960:17</p> <p>sustained [2] - 6927:5, 6951:13</p> <p>sustaining [1] - 6960:6</p> <p>SWAINE [1] - 6773:11</p> <p>swath [1] - 6939:2</p> <p>sweep [1] - 6806:11</p> <p>swipe [1] - 6863:11</p> <p>switch [6] - 6825:24, 6825:25, 6851:3, 6916:5, 6962:21, 6963:15</p> <p>switched [1] - 6920:3</p> <p>swore [2] - 6937:7, 6938:4</p> <p>sworn [1] - 6933:20</p> <p>system [1] - 6813:20</p>	<p>technology [2] - 6794:1, 6794:2</p> <p>TEI [2] - 6828:21, 6829:1</p> <p>telephone [1] - 6938:2</p> <p>ten [4] - 6821:3, 6822:23, 6938:25, 6949:9</p> <p>ten-minute [2] - 6822:23, 6949:9</p> <p>tenants [1] - 6847:22</p> <p>term [4] - 6834:4, 6858:12, 6858:19, 6964:15</p> <p>terminal [2] - 6846:9, 6847:23</p> <p>terminate [2] - 6849:18, 6944:21</p> <p>terminating [1] - 6785:11</p> <p>terms [10] - 6782:8, 6788:7, 6788:8, 6818:9, 6831:8, 6848:20, 6905:25, 6916:6, 6916:8, 6916:19</p> <p>terrible [2] - 6938:17, 6956:18</p> <p>territory [2] - 6809:14, 6809:19</p> <p>test [20] - 6801:3, 6804:14, 6824:25, 6825:6, 6825:10, 6825:19, 6899:21, 6913:14, 6913:15, 6924:6, 6924:11, 6924:16, 6926:17, 6935:25, 6936:1, 6936:2, 6936:4, 6953:2</p> <p>testified [23] - 6780:21, 6784:17, 6786:22, 6787:23, 6795:1, 6803:13, 6815:11, 6821:17, 6821:19, 6825:4, 6836:11, 6856:20, 6856:25, 6857:13, 6867:5, 6867:16, 6871:24, 6882:11, 6916:2, 6917:15, 6917:16, 6941:13, 6953:21</p> <p>testify [1] - 6883:23</p> <p>testifying [1] - 6821:4</p> <p>testimony [31] - 6793:25, 6795:19, 6800:15, 6803:14, 6805:21, 6818:18, 6820:4, 6826:18, 6828:11, 6830:13, 6833:8, 6852:20, 6861:4, 6867:16, 6881:23, 6882:1, 6897:17, 6897:18, 6901:2, 6901:13, 6906:21, 6907:8, 6911:9, 6916:15, 6919:16, 6919:18, 6922:17, 6930:25, 6933:20, 6934:11, 6958:14</p> <p>tests [2] - 6838:9, 6913:18</p> <p>TEXAS [1] - 6772:7</p> <p>text [1] - 6931:25</p> <p>thanking [1] - 6778:13</p> <p>THE [155] - 6774:3, 6774:4, 6774:5, 6774:9, 6774:21, 6775:15, 6775:18, 6776:2, 6776:5, 6776:11, 6776:14, 6776:17, 6776:20, 6776:24, 6777:4, 6777:9, 6777:16, 6777:22, 6778:3, 6778:7, 6778:22, 6778:24, 6779:3, 6779:14, 6779:17, 6780:4, 6788:3, 6789:5, 6790:1, 6790:9, 6791:9, 6796:10, 6796:19, 6796:21, 6796:24, 6797:8, 6797:11, 6797:13, 6797:19, 6801:23, 6802:9, 6802:11, 6802:15, 6808:6, 6808:25, 6809:6, 6809:9, 6809:11, 6809:13, 6809:18, 6809:22, 6813:21, 6814:1, 6814:3, 6814:6, 6814:9, 6814:13, 6816:2, 6816:4, 6818:2, 6818:5, 6818:18, 6818:21, 6818:24, 6821:23, 6822:15, 6822:20,</p>	<p>6822:23, 6823:3, 6823:4, 6823:19, 6831:7, 6833:8, 6833:19, 6833:22, 6834:1, 6834:8, 6839:19, 6840:8, 6840:13, 6841:14, 6841:21, 6846:5, 6847:3, 6847:22, 6847:25, 6862:16, 6864:7, 6865:3, 6865:9, 6865:12, 6865:15, 6865:21, 6866:2, 6866:4, 6875:9, 6885:16, 6885:25, 6886:17, 6886:23, 6890:25, 6891:2, 6891:4, 6891:7, 6891:12, 6898:25, 6909:16, 6914:21, 6915:1, 6915:2, 6915:5, 6915:15, 6925:4, 6938:14, 6938:17, 6938:24, 6946:15, 6946:18, 6946:22, 6946:24, 6947:12, 6947:15, 6947:25, 6948:13, 6948:16, 6948:19, 6948:23, 6949:3, 6949:6, 6949:9, 6949:12, 6949:15, 6949:18, 6949:23, 6952:25, 6953:2, 6954:2, 6954:19, 6955:5, 6955:9, 6955:15, 6955:18, 6956:3, 6956:6, 6956:25, 6961:5, 6961:8, 6961:10, 6961:19, 6962:3, 6966:17, 6966:21, 6966:24, 6967:1, 6967:4</p> <p>theirs [2] - 6871:24, 6895:12</p> <p>theme [1] - 6823:23</p> <p>themselves [8] - 6795:14, 6830:11, 6917:13, 6917:22, 6918:13, 6923:21, 6924:4, 6961:23</p> <p>theoretical [1] - 6817:22</p> <p>theories [7] - 6870:17, 6884:3, 6886:25, 6892:21, 6908:19, 6941:2</p> <p>theory [21] - 6807:11, 6816:23, 6827:4, 6870:24, 6870:25, 6880:18, 6881:24, 6885:4, 6885:23, 6886:1, 6887:7, 6890:16, 6890:17, 6892:8, 6892:10, 6892:24, 6894:12, 6917:4, 6929:11, 6942:12, 6964:11</p> <p>Therefore [1] - 6900:16</p> <p>therefore [4] - 6807:15, 6897:2, 6902:8, 6946:11</p> <p>they've [15] - 6788:15, 6819:20, 6870:18, 6872:25, 6877:13, 6877:25, 6884:3, 6928:11, 6928:17, 6929:14, 6930:4, 6932:8, 6933:21, 6933:22, 6940:9</p> <p>Thiel [3] - 6782:23, 6837:9, 6837:17</p> <p>thinking [9] - 6777:16, 6804:11, 6848:21, 6886:10, 6893:9, 6948:18, 6951:24, 6962:25, 6963:2</p> <p>thinks [4] - 6804:23, 6849:2, 6908:17, 6919:1</p> <p>third [11] - 6805:20, 6815:18, 6819:14, 6839:12, 6863:23, 6891:24, 6891:25, 6917:12, 6921:18, 6931:9, 6961:21</p> <p>third-party [2] - 6805:20, 6819:14</p> <p>thirds [2] - 6920:17, 6931:8</p> <p>thirty [1] - 6920:22</p> <p>THOMAS [1] - 6773:7</p> <p>Thomas [1] - 6774:15</p> <p>thoughtful [1] - 6958:13</p> <p>thousand [1] - 6910:3</p> <p>thousands [1] - 6831:13</p>
T		
<p>T&E [43] - 6797:21, 6827:23, 6829:10, 6829:14, 6829:17, 6829:21, 6830:2, 6830:6, 6832:9, 6832:12, 6832:14, 6833:16, 6835:22, 6838:6, 6838:9, 6853:11, 6854:9, 6854:11, 6854:16, 6854:18, 6854:20, 6854:24, 6855:4, 6855:8, 6855:11, 6904:8, 6905:3, 6912:8, 6920:21, 6920:22, 6921:1, 6925:22, 6926:19, 6926:24, 6927:2, 6927:13, 6927:17, 6927:21, 6928:1, 6928:3, 6929:6, 6965:6</p> <p>table [3] - 6774:10, 6838:11, 6935:4</p> <p>talented [2] - 6957:3, 6957:5</p> <p>talks [3] - 6828:22, 6832:18, 6877:2</p> <p>tampered [1] - 6900:19</p> <p>tampering [1] - 6871:7</p> <p>Target [1] - 6936:20</p> <p>target [1] - 6856:10</p> <p>targeted [1] - 6828:2</p> <p>task [1] - 6929:23</p> <p>taught [1] - 6955:5</p> <p>Tax [2] - 6840:17, 6850:11</p> <p>teach [1] - 6797:19</p> <p>team [3] - 6881:24, 6937:23, 6967:3</p> <p>teased [1] - 6921:15</p> <p>Tech [1] - 6785:16</p> <p>technical [1] - 6782:9</p> <p>techniques [1] - 6933:22</p>		

<p>threat [4] - 6892:25, 6909:8, 6923:24, 6936:14</p> <p>threatened [1] - 6797:25</p> <p>threatening [1] - 6907:11</p> <p>three [35] - 6776:3, 6783:8, 6786:21, 6787:15, 6800:13, 6828:8, 6831:14, 6833:17, 6836:1, 6841:17, 6850:10, 6855:3, 6872:22, 6874:3, 6875:5, 6878:3, 6881:1, 6881:14, 6883:8, 6883:25, 6885:13, 6890:19, 6893:6, 6906:14, 6908:12, 6908:20, 6910:18, 6915:12, 6920:17, 6921:24, 6935:6, 6941:2, 6946:4, 6946:20</p> <p>three-plus [1] - 6941:2</p> <p>three-quarters [3] - 6893:6, 6910:18, 6920:17</p> <p>three-step [1] - 6783:8</p> <p>thresholds [1] - 6782:11</p> <p>thrilled [1] - 6886:20</p> <p>throughout [4] - 6778:15, 6794:10, 6800:20, 6803:13</p> <p>throw [7] - 6842:19, 6913:15, 6913:16, 6916:22, 6916:24, 6917:5, 6917:6</p> <p>thrown [1] - 6792:4</p> <p>Thursday [2] - 6772:17, 6920:14</p> <p>thwarted [1] - 6795:15</p> <p>tick [1] - 6910:14</p> <p>ticket [2] - 6850:14, 6927:12</p> <p>tickets [3] - 6846:14, 6897:10</p> <p>tidbit [1] - 6866:19</p> <p>tinkering [1] - 6871:7</p> <p>tiny [5] - 6866:19, 6867:20, 6867:21, 6910:8</p> <p>today [39] - 6783:11, 6788:20, 6789:23, 6791:17, 6794:16, 6796:5, 6796:8, 6799:10, 6799:19, 6813:15, 6813:18, 6830:19, 6854:3, 6854:7, 6861:4, 6866:15, 6868:5, 6868:8, 6869:14, 6878:21, 6880:3, 6880:8, 6880:11, 6881:21, 6885:14, 6894:3, 6903:15, 6905:8, 6907:22, 6909:19, 6916:21, 6927:12, 6927:25, 6945:23, 6949:20, 6956:12, 6959:22, 6962:17, 6962:20</p> <p>today's [1] - 6869:1</p> <p>Todd [3] - 6801:5, 6801:14, 6876:4</p> <p>together [12] - 6805:5, 6806:11, 6808:23, 6819:14, 6824:15, 6861:19, 6910:21, 6921:15, 6921:21, 6921:22, 6926:23, 6964:21</p> <p>tons [2] - 6904:15, 6909:6</p> <p>took [8] - 6821:23, 6823:10, 6852:2, 6852:6, 6935:12, 6936:8, 6936:13, 6961:12</p> <p>tool [3] - 6779:5, 6924:11, 6965:1</p> <p>tools [2] - 6803:17, 6863:7</p> <p>top [4] - 6806:20, 6853:20, 6908:8, 6908:24</p> <p>Topco [1] - 6899:7</p> <p>topic [8] - 6783:11, 6792:1, 6798:4, 6837:8, 6859:9, 6950:1, 6965:25, 6966:1</p>	<p>topics [4] - 6841:17, 6856:2, 6949:25, 6951:6</p> <p>Tops [1] - 6801:14</p> <p>TORRES [1] - 6772:22</p> <p>total [4] - 6814:19, 6816:18, 6846:10, 6849:3</p> <p>touch [7] - 6783:14, 6802:13, 6823:22, 6841:13, 6841:19, 6949:24, 6965:25</p> <p>toward [1] - 6917:19</p> <p>track [2] - 6839:8, 6921:19</p> <p>tracking [2] - 6905:25, 6921:21</p> <p>Trade [1] - 6875:6</p> <p>transaction [9] - 6806:21, 6863:2, 6863:13, 6879:12, 6879:14, 6879:15, 6927:13, 6927:17, 6927:21</p> <p>transactions [12] - 6804:6, 6805:6, 6805:17, 6805:18, 6805:19, 6806:11, 6862:24, 6880:12, 6931:3, 6931:4, 6931:6, 6940:24</p> <p>transcript [3] - 6772:24, 6905:25, 6962:11</p> <p>Transcript [1] - 6772:25</p> <p>travel [19] - 6797:6, 6799:13, 6799:16, 6831:24, 6832:5, 6833:10, 6833:15, 6834:23, 6835:16, 6836:7, 6836:9, 6836:17, 6837:12, 6838:3, 6839:16, 6857:13, 6889:18, 6925:1, 6925:3</p> <p>TRAVEL [1] - 6772:10</p> <p>Travel [11] - 6827:19, 6828:21, 6829:1, 6829:5, 6829:22, 6829:24, 6831:2, 6832:3, 6851:7, 6854:13, 6964:9</p> <p>traveler [1] - 6836:25</p> <p>travelers [2] - 6837:2, 6838:1</p> <p>Travelocity [3] - 6795:20, 6795:21, 6795:23</p> <p>trend [1] - 6918:3</p> <p>trial [31] - 6778:16, 6778:17, 6778:24, 6779:3, 6781:5, 6781:10, 6801:24, 6804:19, 6811:23, 6813:8, 6815:6, 6820:16, 6820:22, 6821:7, 6835:21, 6838:16, 6851:17, 6856:10, 6856:14, 6856:15, 6856:16, 6858:3, 6862:21, 6866:16, 6869:22, 6901:11, 6929:18, 6944:12, 6948:7, 6952:4, 6962:11</p> <p>Trial [1] - 6820:21</p> <p>tried [9] - 6786:7, 6789:13, 6827:21, 6839:7, 6872:7, 6872:25, 6917:20, 6933:21, 6933:22</p> <p>tries [5] - 6803:25, 6804:1, 6825:20, 6844:19, 6929:25</p> <p>trip [2] - 6929:2, 6929:4</p> <p>troubles [3] - 6798:2, 6798:7, 6798:11</p> <p>true [20] - 6788:20, 6791:21, 6798:2, 6798:22, 6803:11, 6805:19, 6830:22, 6836:23, 6845:4, 6860:8, 6860:9, 6887:11, 6926:18, 6929:21, 6937:7, 6954:8, 6959:4, 6960:13, 6964:5</p> <p>trump [1] - 6803:4</p> <p>truncate [1] - 6865:22</p> <p>trust [2] - 6810:25, 6811:1</p> <p>truth [1] - 6846:19</p>	<p>truthful [2] - 6858:16, 6863:1</p> <p>try [26] - 6804:4, 6810:20, 6812:20, 6815:15, 6819:11, 6823:5, 6823:17, 6833:24, 6834:7, 6850:18, 6856:12, 6860:10, 6860:11, 6860:20, 6860:22, 6861:8, 6861:9, 6866:14, 6868:20, 6884:9, 6932:14, 6934:6, 6949:21, 6959:22, 6963:22</p> <p>trying [15] - 6798:13, 6804:8, 6809:6, 6814:10, 6819:21, 6834:4, 6869:8, 6889:24, 6933:23, 6934:15, 6947:7, 6947:18, 6960:11, 6962:24, 6965:4</p> <p>Tuesday [1] - 6913:22</p> <p>turf [2] - 6797:24, 6798:9</p> <p>turn [10] - 6824:17, 6841:20, 6876:2, 6898:7, 6912:4, 6925:1, 6929:8, 6934:3, 6960:3, 6961:9</p> <p>turnaround [1] - 6868:21</p> <p>turned [1] - 6778:17</p> <p>turning [1] - 6803:18</p> <p>turns [2] - 6833:3, 6960:22</p> <p>tutorial [1] - 6935:6</p> <p>TV [1] - 6898:7</p> <p>Twenty [1] - 6905:12</p> <p>twenty [8] - 6854:3, 6854:4, 6854:6, 6897:2, 6906:2, 6908:3, 6958:3</p> <p>twenty-five [3] - 6906:2, 6908:3</p> <p>Twenty-five [1] - 6905:12</p> <p>twenty-six [4] - 6854:3, 6854:4, 6854:6, 6958:3</p> <p>twice [2] - 6782:24, 6796:4</p> <p>twins [2] - 6893:18</p> <p>two [91] - 6777:24, 6779:12, 6782:8, 6793:19, 6801:24, 6802:20, 6803:9, 6803:11, 6803:16, 6803:22, 6803:23, 6804:1, 6804:7, 6804:17, 6805:2, 6805:4, 6806:6, 6807:20, 6807:24, 6807:25, 6816:9, 6817:6, 6817:12, 6820:13, 6823:22, 6831:14, 6832:24, 6834:13, 6835:25, 6836:1, 6844:5, 6845:14, 6847:8, 6849:22, 6851:3, 6851:24, 6851:25, 6852:23, 6854:2, 6854:4, 6855:3, 6856:1, 6856:4, 6861:1, 6866:10, 6869:13, 6869:15, 6869:18, 6871:24, 6872:1, 6872:3, 6875:19, 6876:19, 6878:12, 6879:8, 6882:4, 6887:15, 6888:9, 6888:14, 6893:20, 6894:2, 6895:10, 6897:25, 6899:4, 6910:21, 6912:7, 6912:15, 6913:9, 6913:14, 6913:17, 6915:11, 6917:1, 6917:9, 6920:17, 6924:22, 6931:8, 6935:11, 6935:12, 6935:18, 6937:15, 6942:3, 6942:5, 6942:7, 6951:11, 6951:25, 6954:18, 6959:2, 6959:6, 6962:14</p> <p>two-sided [20] - 6801:24, 6803:9, 6803:11, 6803:16, 6803:22, 6804:7, 6807:24, 6816:9, 6817:12, 6861:1, 6869:13, 6869:15, 6869:18, 6871:24, 6872:1, 6872:3, 6878:12, 6882:4, 6887:15, 6895:10</p>
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two-sidedly ^[1] - 6844:5 two-sidedness ^[4] - 6802:20, 6807:20, 6820:13, 6823:22 two-thirds ^[1] - 6920:17 type ^[1] - 6801:4 types ^[1] - 6785:5	6857:22, 6858:11 up ^[107] - 6775:19, 6775:21, 6777:24, 6780:9, 6783:12, 6786:24, 6787:5, 6787:10, 6788:16, 6792:16, 6793:2, 6799:22, 6800:3, 6800:8, 6807:12, 6808:15, 6811:3, 6817:20, 6820:2, 6820:11, 6820:21, 6821:8, 6825:16, 6829:20, 6835:21, 6837:6, 6838:16, 6840:3, 6841:25, 6842:24, 6843:4, 6848:8, 6848:14, 6848:22, 6848:24, 6849:24, 6851:5, 6851:23, 6853:20, 6858:1, 6858:22, 6865:6, 6869:25, 6870:2, 6872:16, 6875:22, 6876:11, 6876:13, 6877:10, 6877:14, 6880:6, 6883:1, 6883:8, 6883:23, 6884:1, 6884:20, 6884:22, 6885:2, 6885:5, 6885:15, 6887:6, 6887:10, 6887:12, 6887:13, 6887:20, 6888:9, 6888:13, 6890:17, 6891:10, 6891:12, 6894:22, 6894:25, 6895:11, 6898:1, 6898:5, 6898:20, 6902:9, 6903:12, 6904:22, 6907:25, 6908:24, 6913:20, 6913:22, 6921:25, 6923:18, 6925:9, 6931:1, 6931:22, 6933:23, 6936:3, 6937:20, 6939:3, 6940:17, 6944:6, 6944:8, 6945:25, 6948:8, 6952:14, 6953:8, 6953:19, 6954:14, 6958:2, 6959:19, 6963:1 upper ^[1] - 6853:10 upshot ^[2] - 6785:12, 6834:16 upside ^[1] - 6803:18 upward ^[1] - 6894:24 urge ^[1] - 6863:25 urging ^[1] - 6907:24 USA ^[4] - 6806:3, 6839:5, 6839:18, 6877:17 usage ^[1] - 6905:14 user ^[1] - 6964:17 uses ^[1] - 6964:19 utility ^[1] - 6941:9 utilized ^[1] - 6948:24	variable-contribution ^[2] - 6829:10, 6855:6 variations ^[1] - 6958:4 variety ^[2] - 6830:12, 6830:21 various ^[7] - 6785:5, 6795:11, 6834:14, 6843:11, 6856:17, 6857:20, 6901:3 Varney ^[1] - 6883:18 VButlerRPR@aol.com ^[1] - 6772:24 vein ^[2] - 6855:5, 6959:3 vendor ^[1] - 6908:9 vendors ^[2] - 6928:3, 6945:3 ventures ^[1] - 6796:6 version ^[3] - 6777:1, 6792:6, 6822:17 versions ^[1] - 6829:9 Versus ^[1] - 6785:16 versus ^[7] - 6860:15, 6879:16, 6930:25, 6932:4, 6932:20, 6933:13 vertical ^[8] - 6801:9, 6870:12, 6870:15, 6871:6, 6873:3, 6874:22, 6874:25, 6913:5 viability ^[1] - 6822:1 viable ^[4] - 6779:20, 6781:3, 6930:23, 6954:6 victim ^[1] - 6931:23 VICTORIA ^[1] - 6772:22 view ^[6] - 6817:16, 6820:2, 6820:7, 6820:11, 6913:10, 6919:12 views ^[1] - 6858:25 vigilant ^[1] - 6903:17 violate ^[2] - 6873:24, 6873:25 violated ^[1] - 6864:1 violates ^[2] - 6795:23, 6936:6 violation ^[12] - 6789:23, 6822:2, 6862:13, 6868:18, 6870:8, 6870:10, 6870:16, 6874:13, 6894:19, 6896:18, 6947:2, 6966:15 violations ^[1] - 6874:7 virtually ^[6] - 6851:19, 6869:22, 6932:8, 6934:20, 6939:1, 6941:8 virtue ^[3] - 6791:18, 6860:4, 6910:2 virtues ^[1] - 6951:21 vis ^[2] - 6948:8 vis-a-vis ^[1] - 6948:8 visa ^[1] - 6893:3 Visa ^[110] - 6779:12, 6783:23, 6786:24, 6788:6, 6788:16, 6790:14, 6791:6, 6794:24, 6794:25, 6795:3, 6795:5, 6795:8, 6795:16, 6796:3, 6796:5, 6796:13, 6797:21, 6798:17, 6799:1, 6799:4, 6799:23, 6805:4, 6805:11, 6806:1, 6806:4, 6807:10, 6817:12, 6821:16, 6821:17, 6821:18, 6833:13, 6833:15, 6837:5, 6838:19, 6838:25, 6839:5, 6839:18, 6853:22, 6854:1, 6854:15, 6860:15, 6867:18, 6868:3, 6868:6, 6877:8, 6877:12, 6877:14, 6877:17, 6878:2, 6879:14, 6883:6, 6885:16, 6887:5, 6888:11, 6889:9, 6890:6, 6891:17, 6892:2, 6892:25, 6893:12, 6893:20, 6897:2, 6897:5, 6897:25, 6898:10, 6901:8, 6901:19,	
U	U.S. ^[24] - 6772:9, 6773:2, 6783:23, 6805:3, 6805:11, 6806:1, 6821:17, 6829:3, 6829:12, 6838:19, 6838:25, 6853:22, 6854:1, 6854:15, 6876:13, 6877:7, 6877:12, 6878:2, 6892:10, 6920:9, 6931:19, 6948:6, 6950:8, 6950:22 u.S.A ^[1] - 6773:2 ubiquitous ^[1] - 6930:23 ultimate ^[3] - 6834:15, 6906:6, 6945:4 ultimately ^[1] - 6807:4 unable ^[1] - 6933:15 uncertainties ^[1] - 6822:5 uncertainty ^[2] - 6890:16, 6892:6 under ^[19] - 6783:9, 6783:22, 6811:24, 6813:19, 6816:10, 6817:7, 6819:9, 6819:10, 6824:7, 6845:19, 6853:1, 6858:21, 6867:5, 6870:13, 6871:5, 6873:14, 6873:16, 6883:23, 6937:7 understood ^[2] - 6822:8, 6904:24 undifferentiated ^[1] - 6935:17 unfortunately ^[1] - 6809:15 unilaterally ^[1] - 6863:21 unique ^[2] - 6802:3, 6809:1 UNITED ^[2] - 6772:1, 6772:3 United ^[23] - 6772:20, 6774:8, 6774:11, 6774:13, 6774:14, 6774:15, 6774:16, 6774:19, 6774:20, 6782:19, 6799:21, 6821:18, 6860:15, 6863:13, 6867:6, 6868:16, 6872:20, 6880:8, 6883:19, 6888:17, 6889:23, 6892:17 Universal ^[1] - 6857:18 University ^[1] - 6859:25 unlawful ^[2] - 6873:14, 6952:3 unleashed ^[1] - 6887:14 unless ^[4] - 6777:24, 6917:5, 6938:19, 6966:13 unlike ^[2] - 6888:10, 6939:14 unlikely ^[2] - 6954:25, 6963:16 unmentioned ^[1] - 6818:23 unprecedented ^[2] - 6812:14, 6945:11 unprofitable ^[1] - 6963:16 unreasonable ^[2] - 6873:5, 6951:15 unreasonably ^[1] - 6862:22 unrebutted ^[3] - 6897:16, 6897:18, 6934:11 unremarkable ^[1] - 6899:10 unresolved ^[1] - 6886:11 unsuccessful ^[1] - 6839:20 untrue ^[1] - 6871:4 unwarranted ^[2] - 6817:7, 6882:3 unwelcome ^[4] - 6857:16, 6857:19,	V	vacated ^[1] - 6948:10 vacation ^[1] - 6933:17 valid ^[1] - 6830:3 valuable ^[6] - 6842:17, 6924:11, 6942:23, 6956:22, 6956:23 value ^[43] - 6796:9, 6802:4, 6813:16, 6813:18, 6839:14, 6839:19, 6840:3, 6840:5, 6842:16, 6842:17, 6842:18, 6843:4, 6843:9, 6843:14, 6844:6, 6844:14, 6844:17, 6846:3, 6850:11, 6850:19, 6851:5, 6851:20, 6853:21, 6854:22, 6855:2, 6859:22, 6861:19, 6861:24, 6936:17, 6937:2, 6937:3, 6937:11, 6937:24, 6938:5, 6938:11, 6938:14, 6939:6, 6939:12, 6939:22, 6940:4, 6960:14 variable ^[4] - 6828:22, 6829:2, 6829:10, 6855:6

<p>6903:10, 6903:21, 6903:22, 6904:2, 6904:24, 6906:14, 6908:7, 6909:5, 6910:15, 6910:17, 6910:22, 6916:17, 6917:3, 6917:7, 6920:6, 6920:9, 6921:13, 6921:14, 6921:19, 6921:20, 6927:7, 6930:21, 6931:3, 6931:19, 6932:3, 6932:7, 6940:16, 6940:18, 6940:24, 6941:9, 6941:20, 6941:24, 6941:25, 6945:23, 6946:1, 6947:10, 6950:8, 6950:22, 6954:6, 6956:23, 6959:10, 6959:15, 6959:18</p> <p>VISA ^[1] - 6772:12</p> <p>Visa's ^[2] - 6896:24, 6931:12</p> <p>Visa-MasterCard ^[1] - 6941:24</p> <p>Visa/MasterCard ^[1] - 6872:22</p> <p>visit ^[1] - 6930:9</p> <p>visual ^[2] - 6776:15, 6777:5</p> <p>volume ^[18] - 6786:9, 6788:2, 6792:18, 6799:3, 6839:16, 6850:10, 6850:13, 6867:21, 6880:7, 6892:14, 6909:12, 6911:3, 6913:1, 6918:4, 6922:9, 6924:20, 6924:21, 6931:12</p> <p>volumes ^[1] - 6922:19</p> <p>voluntarily ^[1] - 6934:1</p> <p>Vons ^[1] - 6913:4</p> <p>vulnerable ^[3] - 6828:2, 6831:4, 6832:13</p>	<p>week ^[3] - 6778:16, 6778:24, 6952:4</p> <p>weeks ^[4] - 6778:18, 6891:2, 6915:12</p> <p>weight ^[5] - 6820:22, 6894:8, 6953:18, 6961:10, 6961:21</p> <p>Weiss ^[1] - 6775:10</p> <p>WEISS ^[2] - 6773:19, 6775:10</p> <p>welcome ^[9] - 6856:5, 6856:7, 6856:19, 6857:8, 6858:12, 6858:14, 6858:19, 6859:5</p> <p>Welcome ^[2] - 6902:4, 6902:12</p> <p>welfare ^[1] - 6944:12</p> <p>well-being ^[1] - 6867:23</p> <p>well-established ^[1] - 6824:7</p> <p>well-known ^[1] - 6830:10</p> <p>Wells ^[3] - 6805:20, 6833:13, 6833:15</p> <p>Wendy's ^[3] - 6927:25, 6928:6, 6928:7</p> <p>wheel ^[1] - 6795:4</p> <p>whereas ^[1] - 6915:5</p> <p>whole ^[14] - 6794:10, 6802:17, 6806:22, 6806:23, 6832:23, 6833:5, 6848:25, 6850:13, 6850:21, 6869:15, 6877:25, 6939:1, 6965:5, 6965:23</p> <p>wide ^[8] - 6780:25, 6800:16, 6831:13, 6831:17, 6899:24, 6900:2, 6939:2, 6957:6</p> <p>widely ^[2] - 6828:12, 6828:13</p> <p>willing ^[3] - 6780:3, 6848:10, 6916:5</p> <p>win ^[1] - 6811:21</p> <p>window ^[3] - 6778:25, 6858:4, 6858:7</p> <p>winds ^[1] - 6825:16</p> <p>wipe ^[1] - 6794:15</p> <p>wiped ^[1] - 6850:18</p> <p>wish ^[2] - 6837:20, 6944:10</p> <p>withdrew ^[1] - 6842:15</p> <p>WITNESS ^[1] - 6968:3</p> <p>witness ^[8] - 6867:4, 6869:3, 6871:23, 6897:19, 6901:24, 6942:6, 6942:7, 6942:11</p> <p>witnesses ^[9] - 6778:19, 6778:20, 6780:7, 6856:17, 6893:19, 6897:17, 6916:15, 6922:15, 6929:21</p> <p>woke ^[1] - 6913:22</p> <p>won ^[3] - 6887:19, 6898:6, 6936:4</p> <p>wondering ^[1] - 6947:25</p> <p>word ^[7] - 6847:16, 6872:18, 6872:23, 6906:17, 6926:14, 6941:18, 6953:3</p> <p>words ^[6] - 6777:20, 6862:10, 6872:24, 6876:14, 6878:3, 6951:10</p> <p>workaround ^[1] - 6793:21</p> <p>works ^[10] - 6781:9, 6786:13, 6791:20, 6819:18, 6832:19, 6835:14, 6840:15, 6849:12, 6881:12</p> <p>world ^[21] - 6789:3, 6817:23, 6861:24, 6883:7, 6885:4, 6885:15, 6890:16, 6890:18, 6892:20, 6918:11, 6918:19, 6920:12, 6921:3, 6922:5, 6923:4, 6931:15, 6944:5, 6954:7, 6954:23, 6959:10</p> <p>Worldwide ^[1] - 6773:11</p> <p>worried ^[4] - 6792:17, 6793:23, 6833:20, 6907:21</p>	<p>worry ^[2] - 6808:13, 6827:6</p> <p>worse ^[2] - 6870:7, 6894:4</p> <p>worth ^[3] - 6842:10, 6849:2, 6849:3</p> <p>worthless ^[1] - 6843:1</p> <p>worthy ^[1] - 6936:1</p> <p>wound ^[1] - 6933:7</p> <p>write ^[2] - 6817:22, 6940:6</p> <p>writing ^[1] - 6905:20</p> <p>written ^[2] - 6871:8, 6894:6</p>
W		
<p>wait ^[2] - 6883:16, 6884:6</p> <p>wake ^[1] - 6868:3</p> <p>Walgreen's ^[2] - 6910:19, 6910:23</p> <p>Walgreens ^[3] - 6909:16, 6909:17, 6910:25</p> <p>walk ^[3] - 6810:1, 6911:7, 6945:10</p> <p>walked ^[2] - 6856:15, 6908:13</p> <p>walks ^[1] - 6944:19</p> <p>Wall ^[1] - 6883:14</p> <p>wall ^[1] - 6898:8</p> <p>wallet ^[4] - 6792:6, 6792:8, 6792:9, 6898:8</p> <p>wallets ^[3] - 6792:5, 6891:20, 6920:13</p> <p>wants ^[14] - 6784:6, 6801:7, 6806:10, 6807:14, 6813:9, 6814:25, 6817:13, 6832:6, 6837:17, 6908:18, 6933:19, 6940:23, 6963:20</p> <p>war ^[1] - 6938:8</p> <p>Warehouse ^[5] - 6875:20, 6882:23, 6899:20, 6900:9, 6912:16</p> <p>warped ^[1] - 6810:21</p> <p>Washington ^[3] - 6773:4, 6908:2, 6942:18</p> <p>watching ^[1] - 6952:14</p> <p>water ^[2] - 6829:15, 6850:22</p> <p>ways ^[12] - 6784:19, 6790:7, 6795:11, 6814:11, 6819:5, 6820:10, 6835:20, 6838:2, 6838:25, 6843:11, 6866:12, 6915:17</p> <p>weaken ^[1] - 6901:15</p> <p>weaknesses ^[1] - 6778:25</p> <p>wear ^[1] - 6879:8</p>		
X		
x-rays ^[1] - 6952:1		
Y		
<p>yards ^[1] - 6869:7</p> <p>year ^[7] - 6851:22, 6851:23, 6884:8, 6884:9, 6884:10, 6908:14, 6913:2</p> <p>years ^[42] - 6791:16, 6803:16, 6807:8, 6810:4, 6821:4, 6840:6, 6840:19, 6840:24, 6860:11, 6867:3, 6868:10, 6870:4, 6870:10, 6872:23, 6873:13, 6883:8, 6884:5, 6884:10, 6889:21, 6889:23, 6890:19, 6894:10, 6898:6, 6901:12, 6901:23, 6905:5, 6905:10, 6906:9, 6906:14, 6908:3, 6908:21, 6920:10, 6923:16, 6928:14, 6936:8, 6939:1, 6940:4, 6946:4, 6946:7, 6958:2, 6962:21</p> <p>yellow ^[1] - 6829:12</p> <p>YORK ^[1] - 6772:1</p> <p>York ^[14] - 6772:23, 6773:12, 6773:16, 6830:16, 6830:20, 6832:1, 6832:7, 6912:16, 6928:23, 6928:24, 6928:25, 6965:15</p> <p>York/Chicago ^[1] - 6831:15</p> <p>young ^[1] - 6902:19</p> <p>yourself ^[4] - 6796:17, 6833:6, 6859:3, 6960:7</p> <p>yourselves ^[1] - 6775:22</p> <p>yup ^[1] - 6940:10</p>		
Z		
zero ^[3] - 6852:17, 6914:18, 6933:21		